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THE TWO RADICALLY DIFFERENT CONCEPTS OF

Utility "Depreciation"

I. What it means in accounting practice

In valuation proceedings, the term means one thing; in accounting work it means another. The two concepts are entirely different and bear no necessary relation to each other in the case of utility properties. This is the first of a series of two articles on a subject which has a direct bearing upon utility rates.

BY HENRY EARLE RIGGS

ONE of the most controversial of subjects in connection with the regulation of public utilities is that which deals with the proper accounting for the retirement of units of property which will be taken out of service for any reason.

Many of the engineers, operating officials, lawyers, and judges who are called upon to deal with rate making or valuation find the subject clouded in mystery, and find to their surprise that violently conflicting opinions are held not only by engineers, but also by skilled accountants and administrative officers of the large utility companies.

A number of years ago the writer set out to try to find out for himself what it was all about and to discover the relative merits of the various arguments that were being advanced. Much to his surprise he found that while the use of accounting reserves for various purposes had been in vogue for many years, the term "depreciation reserve" was of very recent origin, and the so-called "straight-line" method, or theory, is a very late development.

Recent discussion of so-called "depreciation reserves" in connection with the proposed accounting rules

for telephone companies and railroads, and the final order of the Interstate Commerce Commission, give great present importance to the subject.

It is unfortunate that the word "depreciation" has been applied to two radically different concepts.

In valuation work, "depreciation" should be defined as a subnormal or run-down condition of a physical plant —one which is below the proper maximum condition in which the plant can be and should be permanently maintained in order to render adequate service. The courts hold consistently that this depreciation, if any exists, must be found and deducted from value for rate-making purposes.

In accounting practice the word has come into recent general usage to represent the amount which should be reserved out of earnings in each fiscal period to cover the loss of service life in that period so as to provide for the retirement of property units when they come to the end of their service lives. The use of the word "depreciation" in this connection is misleading and confusing. The true purpose of this form of accounting is to spread the cost of long-term property units over the revenue they assist in producing. The use of the word "depreciation" undoubtedly is due to the fact that just at the time this form of accounting was developed many state valuations were being made, and the attempt was made to offer it as a plan for making good the depreciation found in valuation.

These two concepts of depreciation are entirely different, and bear no necessary relation to each other in the case of public utility properties of continuing an indefinite life. Accounting rules that may be, and probably are proper in the case of manufacturing property, or single properties such as office buildings, hotels, or other unregulated properties, which are under no obligation to continue service, are not necessarily applicable to regulated continuing properties.

There must be a sharp distinction between these two concepts, and they must not be confused when either one is under discussion.

This article deals with the subject of accounting; therefore, no thought of valuation must be allowed to intrude. Depreciation of valuation is another story.

The use of the word depreciation to express two wholly different and unrelated things, together with the many efforts that have been made to clarify the subject by coining various words and phrases to express different shades of meaning in connection with discussion of the subject, are largely responsible for the general misunderstanding of the subject by those who have only occasional touch with it.

To understand the subject, let us review the history of accounting reserves for the retirement of property:

Books on accounting are in existence printed in 1675 and in 1744, both of which treat "wear and tear" as an expense, and treat the item on the balance sheet as a contra account, deducted on the asset side.

The writer has found occasional references in the period between 1800 and 1840, which indicate that reserves or annuities for the retirement of

physical plant were not infrequently used.

Between 1845 and 1855 the subject of depreciation of railroads received the attention of special commissions in England and Holland. In 1848 the legislature of Massachusetts passed a law requiring railroad companies in making reports to the legislature to report depreciation of rails, structures, and equipment. In 1850 a similar law was passed in New York. These laws were generally disregarded by the railroads and only a few such reports were made.

In 1850 Harper & Co. published a volume by Dionysius Lardner entitled "Railway Economy"; in this book the author argues that after twenty years' experience in operating railroads it is obvious that it will be necessary to replace railroad track in its entirety every twenty years.

In the annual report of the state engineer of New York in 1855 attention is called to the failure of the railroads to report depreciation, and this significant paragraph is used:

> "It is contended by many skilled managers that if the works and rolling stock are kept in thorough repair, they are in as good condition at the end of each year as they were at the end of the preceding year, and, therefore, that there can be no depreciation."

Thus it appears that eighty years ago the same problems existed that we now contend with, and some of the same arguments were advanced. There was no reference in any of these early reports to any form of reserves other than "annuities," or sinking-fund reserves.

In October, 1878, in United States *v.* Kansas P. R. Co. (99 U. S. 455, 25 L. ed. 289) the United States Supreme Court in the first decision touching this subject declared that a "depreciation account or expense not charged up" was not a proper charge to operating expenses and said: "Only such expenditures as are actually made can with any propriety be claimed as a deduction from earnings."

When conditions of those unregulated times are considered, it is easy to see why the court placed this sort of a restriction on charges to operating expenses.

It was not until 1909 in the Knoxville Case and the Cumberland Telephone Case that the court recognized the propriety of providing for retirement through reserves.

Prior to 1897 the waterworks industry began to develop reserve accounting under the name of "depreciation reserves." Transactions of the American Society of Civil Engineers in that year contain two papers which refer to the subject, one of which de-

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scribes the sinking-fund plan of reserve accumulation. In October of the same year the supreme court of California held against the establishment of a depreciation reserve, following the precedent of the Kansas Pacific Railroad decision.

ACCOUNTING practice prior to 1900 may be summed up by stating that there was no general recognition of a necessity for reserve accounting, and only occasional use of the plan of annuities for this purpose. The so-called "straight-line" method was not used generally in accounting, if at all.

RETIREMENTS of plant have been treated in different ways by the different utilities. Railroad way and structures have been maintained by directly charging retirements or replacements to operating expenses as they occur, without the use of reserves. The same procedure has prevailed on some other properties. Occasionally reserves are created to spread the cost of major retirements over several years. The telephone companies have consistently used reserve accounting for all retirements. By far the greater part of all investment in public utility plant is owned by companies which use reserve accounting to only a limited extent.

The amortization of investment in a property which will definitely cease to exist at a date that can reasonably be determined; the equalization of large retirements over a period of years in order to maintain a uniform ratio of expenses to earnings; or the establishment of a maintenance reserve that will serve the purpose of permitting the company to lay aside in prosperous years sufficient reserves to permit full and adequate maintenance in lean years, are legitimate reasons for establishing reserves.

Properties such as the great railroad systems, electric power properties, waterworks, and other continuing utilities, do not need to amortize their investment in plant. Capital is not being withdrawn from such properties, but on the contrary they are continually seeking new capital. It is the duty of such a company to maintain the plant devoted to service so that it will always be in condition to give safe, ample, and efficient service. Reserves which are established on any theory that provides for amortizing all of the units of such a property are greatly excessive. Reserves which are established on the theory that each year, or each month, must bear its equal share of the cost of retirement of the property are improper because they neglect the equally important function of caring for fluctuations in business. Such reserves instead of being beneficial constitute a burden, and, especially in times such as these, destroy credit instead of preserving property.

FROM the standpoint of public interest and public regulation of utilities the manner of creating the reserve is of great importance. Patrons of a utility should concede the right of the company to have ample rates to permit the property to be kept in fully adequate condition to give service and to pay a liberal return on the value of the property. Patrons have a right to insist, however, that accounting methods shall be used which can be readily checked and which

When the Term "Depreciation" Is a Misnomer:

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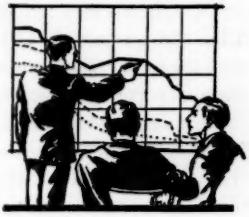

correctly state the true net earnings. Any accounting device that tends to conceal actual expenditures for maintenance or retirement or that makes it possible to overstate expense should, therefore, be used under the most rigid regulation.

Reserves created by appropriations of surplus are, therefore, not at issue as the company owns the surplus and may do with it as it pleases. The reserves that should be subjected to rigid scrutiny are those that are created by charges to operating expenses.

It is interesting to find that some of our learned state and Federal judges have been confused as to the effect of charges to operating expenses for so-called "depreciation." The statement was made in one case that they were "mere bookkeeping entries" and did not represent any actual transaction.

Let us see what really happens.

If a charge of $1,000 is made to operating expenses for "depreciation" and a corresponding credit is made to a so-called "depreciation reserve," the practical result is that $1,000 is withheld from gross earnings and at once becomes available to the company either for making new capital investment, payment of current liabilities, or any other legitimate corporate use except dividends.

It must be pointed out that this accounting transaction of charging to operating expense and crediting reserve does not establish a depreciation fund or set aside the money for any specific purpose. Either a "reserve" for depreciation or a "fund" for the same purpose may exist without the other.

A "fund for depreciation" represents money specifically set aside for that purpose, and if that is to be done there must be another accounting transaction than that just described in connection with the reserve. A fund appears on the asset aside of the balance sheet and represents a definite appropriation for a certain purpose.

There is disagreement among accountants as to the proper balance sheet treatment of the "depreciation reserve." One group contends that it should be carried on the liability side of the balance sheet as a deferred liability. Another group, including a majority of the authors of books on accounting, hold that it

should appear on the asset side, as a contra item to be deducted in finding the net worth of the assets.

So far as this article is concerned, the charge of $1,000 to operating expense and the credit to "depreciation reserve" results in the company *having* the thousand dollars to spend, and in reported net earnings being reduced by that amount.

Both the regulating commission and the patron who pays rates for service are interested in knowing whether or not such a charge to operating expense is proper. If not, the result is a concealment of net earnings.

DURING the past five or six years the Interstate Commerce Commission has been considering a revision of railroad and telephone accounting. Many hearings have been held. Orders and revised orders have been issued. Volumes of discussion have been printed. In its order the commission prescribes the same accounting treatment for two dissimilar industries which have in the past used wholly different methods of accounting for the maintenance of their properties. The remedy that is prescribed for all ills is compulsory "depreciation reserves" computed in accordance with the "straight-line" plan. That is, if a unit of property has a "life" of fifty years, 2 per cent of its cost is charged to operating expenses each year. If its "life" is five years the charge will be 20 per cent. No better description of this plan can be found than that of Mr. Commissioner Eastman in 118 Inters. Com. Rep. 295, 353 to 356, where he compares it with the sinking-fund plan.

The hypothetical character of the estimate appears on page 353. The writer quotes it, using italics to emphasize his point.

> "First of all, the total depreciation expense is determined by *estimating* the 'service value' of the property in question. This requires not only a ledger value *corresponding as nearly as may be* to original cost, but also an *estimate* of 'net salvage value' at the time of prospective retirement and a similar *estimate* of 'service life.' Finally the annual depreciation charge is determined by *dividing* the *estimated* service value by the *estimated* service life. The purpose of this method of determining depreciation charges is to spread the entire expense evenly over the life of the property in service."

It is appropriate at this point to find out where the "straight-line" plan originated.

A STUDY of the annual reports of the American Telephone and Telegraph Company from 1895 to 1930 furnishes conclusive proof that this company had a very large part not only in the development of this plan of accounting but also in bringing about a general recognition of so-called "depreciation" accounting. For many years the company has included very full discussion of its plans, policies, and public relations in its reports, a practice which in large part accounts for the enviable position which it holds among public utilities.

The company commenced setting up reserves very early in its history. From 1900 to 1906 the balance sheets show a liability account captioned "reserves" but in these years the word "depreciation" does not appear in its operating expense statements. The report for 1907 refers to a valuation of property by the company. The report for 1908, under the caption "depreciation" refers to reserves for

this purpose and the annual rates to be used in computing them. In the report for 1907 and the two succeeding years operating expense accounts are captioned "maintenance and depreciation," and in 1910 there was a division into "current maintenance" and "depreciation." In the balance sheets the liability account was captioned "depreciation reserve" from 1907 to 1912.

The annual reports of 1910 and 1911 discuss the theories of the company at great length and are among the best early expositions of the subject of depreciation that are to be found.

A study of these reports and of the early accounting circulars of this company make it clear that the subjects of property valuation and accounting methods received the most careful attention and that the company definitely undertook to establish accounting precedents for the telephone industry.

"ACCOUNTING Circular No. 6," issued by the American Telephone and Telegraph Company in November, 1909, was evidently the model used by the New York commission in the preparation of its telephone classification which became effective January 1, 1912, and which in turn was adopted with very minor changes by the Interstate Commerce Commission as the basis of its classification of telephone accounts effective January 1, 1913, and still in effect.

Thus it appears that the telephone utility anticipated the regulation of its accounting methods and put its house in such order that it was able to secure the adoption of its own accounting plan with very minor modifications as the official plan.

The company has consistently followed the "straight-line" formula, and has built up reserves by yearly charges of somewhat more than 5 per cent of the total ledger value of the plant until very recent years, when the annual allowances have been reduced to slightly less than an average of 5 per cent.

The fact that this method has been highly successful with the prosperous telephone company, that its use has built up large credit balances in the reserve, and that it has not been subjected as yet to serious criticism, does not necessarily prove its soundness or its applicability to all forms of regulated utility property.

LOOKED at from the standpoint of regulation of utilities, this method is open to many and serious criticisms. Some of these may briefly be stated as follows:

I. It substitutes estimates as to probable "service life," probable future salvage value, and probable

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service value, for the accurate recording of actual cost of maintenance and retirements in charges to operating expenses.

2. It will destroy the statistical value of the operating expense accounts, and compel the publication of the full detail of charges to the reserves in order to permit analysis of actual expenditures. The adoption of an accounting plan which requires arbitrary charges to operating expense for estimated "depreciation" will destroy the comparability of past and future statistical records, past statistics being based on accounting records of actual cost of maintenance and actual retirements.

3. The plan depends wholly on "life tables," which can be discussed at great length without developing much proof of their accuracy or sound reason for their adoption.

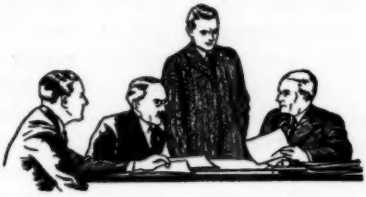
4. The use of "straight-line" reserves, even when intelligently and conservatively estimated, results in building up immense credit balances, far in excess of any reasonable requirement. If these credit balances be deducted from plant there can be little or no objection to their size. If it be assumed that the company will in the near future cease business and liquidate there would be a sound reason for such balances. For example, the New York Telephone Company has had a credit balance in the reserve during the past twelve years which was in excess of 25 per cent of the ledger value of fixed capital.

5. There is grave danger of the misuse of this accounting device for the purpose of deliberately overstating operating expenses and concealing true net earnings. The discussion of secret reserves by Professor Henry Rand Hatfield on page 142 of the 1926 edition of "Accounting," goes directly to this point. It has already been shown that the result of the charge to operating expense and the credit to the reserve is to make available to the company the use of a like amount of money. If the charge to operating expenses is excessive, whether deliberate or unintentional, the result is a concealment of earnings.

6. The mandatory reserves prescribed by the Interstate Commerce Commission in its recent order, based on a percentage of property value, give no regard to fluctuations of business or earnings which are inevitable owing to seasonal variation in volume of business, or to changing economic conditions. A couple of years ago the president of one of the large utility companies made a statement in a letter to the writer which goes directly to this point, as follows:

> "My disagreement with you does not mean that I accept the foolishness of the doctrinaires who persist in teaching that each year of our Lord is a person-at-law having rights and sanctions as against every other year, in respect to accruals of depreciation, whether the same be proven by inspection or be estimated by some scholastic formula. I insist on providing for accruals which I know must inevitably accrue. But I propose to follow the rule which was good business when Joseph was grain controller to old Rameses —namely, to make the good years contribute to reserves or to betterments which will maintain value, and to let the lean years travel into the past without marking them as defaulters."

7. Such a plan, which might be wholly acceptable to the rich and prosperous companies in any utility,



The Necessity of Regulating the Manner of Creating Reserves

"FROM the standpoint of public interest and public regulation of utilities the manner of creating the reserve is of great importance. . . . Any accounting device that tends to conceal actual expenditures for maintenance or retirement or that makes it possible to overstate expense should be used under the most rigid regulation."

would inevitably be disastrous to those with small earnings. Were the commission's plan in effect now, it would in all probability so seriously injure the credit of many of the smaller railroad corporations as to result in widespread bankruptcy.

8. The use of the straight-line plan disregards interest. The accumulation of hundreds of millions [1] of dollars in reserve balances under the straight-line plan gives the owning company the use of that money without the payment of any interest therefor. In the case of one telephone company proof was offered in a recent rate case that the company had saved interest expense to itself amounting to over fifty million dollars computed at 5 per cent, without compounding, in a period of fifteen years.

9. The Interstate Commerce Commission says that "it is essential to bear in mind, however, that there is an inseparable connection between the straight-line method and the principle that accrued depreciation represented by the depreciation reserve must be deducted in ascertaining the rate base value." [2]

The Federal court on November 7, 1929, said:

> "But if the actual depreciation exists to the extent that the plaintiff has claimed in building up this reserve, it exists as much for valuation purposes as it did for the creation of the surplus." (36 F. (2d) 54, P.U.R.1930B, 33.)

It is impossible to get away from the soundness of this doctrine. The cold fact is that companies which have "straight-line" reserves have created them on the theory that an

[1] The 1930 statistics of the Interstate Commerce Commission show that depreciation reserves of the railroads as of December 31, 1930, aggregated $2,360,766,740, the increase for the year being $191,030,574. The 1931 annual report of the American Telephone and Telegraph Company shows reserves for the Bell system of $788,586,005, the increase for the year being $48,580,130. The above figures show reserves of 9 per cent of railroad book value and 18.4 per cent of telephone book value.

[2] (118 Inters. Com. Rep. 295, 356.)

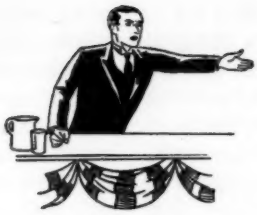
economic hole is being made in utility property every year, and they have actually collected the money from the ratepayer to fill that hole. A number of such companies have attempted to adopt the argument of the railroads, which have not created reserves for roadway and structures, and have not collected the money for this purpose through charges to operating expense. The railroads properly object to a deduction for depreciation based on the computation of a hypothetical straight-line reserve that was never created and collected. It appears entirely reasonable to expect that if this form of reserve accounting is to continue it will be under the restriction placed by the commission; when the users of the plan refuse to recognize the restriction, the use should be discontinued.

MUCH more might be added to this discussion. We might with propriety discuss the effect of changing prices on the reserve estimates. We might discuss the Supreme Court's decision in the Baltimore Case, which knocked into a cocked hat the academic theory of the Interstate Commerce Commission, and we might quote at length from the opinions, not of the railroad accountants who are all opposed to the theory, but of the elder statesmen in other utilities. Companies of the highest standing such as the Consolidated Gas Company and the Detroit Edison Company oppose this plan of reserve accounting and have voiced their opposition in no uncertain terms.

The writer believes that the Interstate Commerce Commission, when it promulgated its recent accounting order, opened a Pandora's box of troubles the like of which have never before been loosed to plague the various utility commissions and to start untold investigations and litigation. It is unfortunate, but true, that the sickly, weak, and decadent companies—the ones that need to amortize their investment—have not been able to earn enough to do so in the past on any plan, and can hardly be expected to do so at present.

Those companies which have built up large credit balances in reserves, using this method are bound to face the fact that the reserves are not *depreciation reserves* and do not represent the true existing depreciation in the properties but are in effect retirement reserves which in effect amortize capital. They compel an annual charge against the consumer much greater than is necessary to provide a sinking fund to retire the plant. They result in great reservoirs of cash on which the company pays no interest but invests in property on which it demands a return.

WERE these "straight-line" reserves accepted as the measure of depreciation in the rate base of all companies which have used this form of accounting and collected the money through the rates, it is not probable that any serious question would be raised. The argument is made, however, that reserves do not measure depreciation. This fact, and the actual existence of reserves aggregating hundreds of millions of dollars in the case of some industries leads to the belief that investigation of this subject of reserves by the public is inevitable in the light of present conditions.



THE MACHIAVELLIAN PLOT BEHIND

The Barrage of Ballyhoo

The ulterior purpose of the utility barons in stimulating the vice of verbosity in their critics while they themselves commit the sins of silence, as reported by—

RAYMOND S. TOMPKINS

My snoopers bring me word of a new and more diabolical plot hatched by the robber barons of the public utility business and their vassals, the publicity men.

I know that this will not be believed. No one, to be sure, will have any doubt that they have hatched up something new, but few will believe that they have produced anything more diabolical than their schemes to poison the well-springs of learning in this country, ravish the public school textbooks, devour America's sacred birthrights, and set up a government of utility autocracy.

But whether my new information is believed or not, I hasten to make it public. I could keep it locked within my breast if I wanted to, and get many a private chortle out of it as I waited for things to materialize, but I know perfectly well what would happen to me when they *had* materialized; how every tortured cry of every widow and orphan would cut me like a knife, how the sound of the loaded tumbrils rolling through the streets would tear me mentally to pieces like the rumble of doom. Even now, so long as I keep this secret, the prattle of unsuspecting children makes my blood run cold.

I am, therefore, baring everything so that the country may spring to arms in time if it believes the story. If it doesn't believe it, let it go to the devil in its own way.

This is the plot: The publicity men of the power and light industry, presumably the soundest and most expert practitioners of their art, are at an early date to steal across into the enemy lines and by various disguises and tricks get themselves established at Anti-Power Trust headquarters as friends of the Anti-Power Trust movement. Their luxurious offices in elegant penthouses on the peaks of the country's most appalling skyscrapers are to be perma-

nently closed and locked. Not a line of mimeographed copy or a sheet of flimsy will issue from them. For all they care the first grade textbooks on history can picture George Washington indignantly chopping down a privately owned electric light pole; they can say the slaves Lincoln freed were really a crowd of innocent householders locked up in dungeons by the Power Trust because they couldn't pay their exorbitant electric light bills. Indeed, the more of this kind of thing the textbooks burst out with, the better for the fiendish purposes of these unscrupulous gentry, as we shall soon see.

Their aim now will be to worm their way into the confidence of the leaders—men like Pinchot, Franklin Roosevelt, Norris, Walsh, and so on. This will not be difficult, for these gentlemen burn with eagerness to help humanity, and anybody with a new idea in that direction can have their ears at once and their shirts as well. The utility wolves in sheep's clothing will, of course, be full of ideas helpful to humanity, and these fine fellows will soon be eating out of their hands.

And what will they be eating?

That, my friends, is the nub of the whole plot. That is what gives you the shivers like seeing a woman sawed in half; covers you so thoroughly with goose-bumps that blind men start reading on you like a Braille System magazine.

They will be consuming publicity advice, so plausible, so pleasant, so logical, and yet, withal, so wicked in purpose as to be well-nigh incredible. Small wonder that the Senators and governors will be listening to it, for selling publicity campaigns is the vocation of these utility publicists and they are very adept at it. They can take a careful, quiet public utility executive and turn him into a roaring lion as full of sonorous self-righteousness as a back-lot evangelist, and with just about as much sense. They can take a smart and sensible utility leader, and make a radio broadcaster of him. So it is easy to see what saps they will be making of our friends who burn for humanity.

FIRMLY established in their confidence, these rascals will be whispering to the governors and Senators that their attacks on the Power Trust and on regulation have been entirely too temperate; that this is the reason the utility pirates have not yet been blown out of the water entirely. The senatorial speeches have been too mealy-mouthed. The gubernatorial campaign red fire has been too pale and pink. There hasn't been enough old-time hell's-fire and damnation. That's what the people want, the unspeakable scamps will be hissing into the ears of the people's choices. With the same fiendish flair for words that has permitted them to bamboozle a gullible American public, they are to suggest hotter phrases, more sizzling similes, frightfuller denunciations, fiercer charges of wickedness and corruption.

They are to do all this knowing full well that their noble victims will swallow the stuff hook, line, and sinker; knowing also that the whole plan will enable the wicked utilities to "beat the rap," go scot free, escape all punishment with absolute certainty.

Is the scheme now plain? Could anything be clearer? Could any plot be crueler; any set of men more deliberately vicious?

For, as students of the most fundamental principles of public psychology, the utility gents (as well as all of us), are thoroughly familiar with these simple truths:

(1) That intemperate and fanatical attacks upon anybody or anything are bound to fail and always have failed in America;

(2) That most attacks upon the power and light industry and upon the regulation of it are already failures because of their intemperance and fanaticism;

(3) That the more intemperate they grow the quicker the failure will be completely apparent, and

(4) That the longer the current serious and solemn defensive publicity against these windy and ridiculous Power Trust charges continues, the longer the attacks will continue.

THAT is the plot as my *agents provocateurs* have unmasked it. It means a swift end to the battle against the utilities, death to the Anti-Power Trust movement, freedom for the development of sound regulation, a little spell of peace and quiet. So to arms, fellow countrymen, unless you yearn for the rattle of the chains and the crack of the bullwhip about your ears!

Personally I think, if this is all true and my spies have not been taking me for a ride, that the utilities of this country are showing in this plot the first feeble symptoms of sound horse sense since the present "war," as Governor Roosevelt calls it, was begun. It means that they have thrown into the ash-can the philosophy of utility leaders, particularly the expert publicists who are constantly decrying the industry's "sin of silence," and baying deep-mouthed demands that the power and light business proclaim its purity. Honest and well-meant as this philosophy is, it is also the philosophy of the common thief, as even the stupidest citizen knows. The first instinct of the criminal accused of crime is to shout that he is innocent; it is expected of him by everybody and gets exactly the credence it deserves, which is none. Once in a great while some genius in the understanding of public psychology like George Washington comes along, and instead of denying the crime, admits it boldly and even tells how he did it. He is promptly made president and canonized as a saint.

Naturally, if too much of that sort of thing were done, the followers of the cult would become a public nuisance and be clapped into jail where they belong. I do not here recommend that guilty people go around boring everybody to death with loud

¶ "TRYING *to get John Quincy Public interested in improving his lot by a holy war to reduce his gas and light bill, is like advising a man with arthritis, stomach ulcers, gall stones, cirrhosis of the liver, and baldness, that the way to begin restoring his health is to use a good hair tonic.*"

proclamations of their guilt. I merely set forth for public utility publicists the simple truth, already well known to themselves, if they stop to think about it, that to answer charges of guilt with nothing but protestations of innocence is to do so obvious, so commonplace, and so expected and uninteresting a thing as to be thoroughly conspicuous and hence subject to all manner of inspection and suspicion. More of the "sin of silence" and less of the "vice of verbosity"—perhaps the industry needs this.

At any rate, the primeval reactions of the common criminal are unworthy of men as intelligent and resourceful as the leaders of the utility industry. It will be answered that these are also the instinctive reactions of innocent men wrongfully accused of crime, and proclamations and proof of innocence are required of them in courts of law. This brings me to my point, for the answers to the above are:

First, that the accusations of the Anti-Power Trust evangels are not, in the proper sense, accusations at all, but amount, in their entirety to the most gigantic free exhibition of shadow-boxing and bag-punching that the nation has ever been treated to, and;

Second, that the utilities are not in a court of law, at all, but in a court of public opinion, where fanaticism, oratorical intemperance, and political nonsense have the same familiarity and propriety as the tarlatan skirts of a lady bareback rider in a circus, and are just as transparent.

Let me here quote very briefly from some of the least opaque of the remarks of some of the country's busiest dragon slayers:

"The Power Trust was given the greatest victory (election of Hoover), since it began the stealthy and secret attempt to control all the activities of our economic and political life."
(Senator Norris, November 11, 1928.)

"The Power Trust was given the soundest licking (elections of Roosevelt and Pinchot), since it began," etc., etc.
(All the Anti-Power Trust spokesmen, in 1930.)

"The greatest sufferers (from extortionate electric rates), are the women. . . . In this country woman must either perform this household drudgery herself or hire someone else to do it. If the Power Trust would at least reduce rates by the amount they now spend in deceiving their customers, one mark against them would be erased."
(Senator Norris, December, 1928.)

"I want to help break the strangle-hold of the electric, gas, water, trolley, bus, and other monopolies on the cost of living and the government of this state."
(Governor Pinchot, campaign speech, March, 1930.)

"Today in this field of war two armies are drawn up, one seeking to break down the distinctions between the utilities and other forms of industry seeking to free the utilities from all limitations of profit for personal gain, and on the other side that more modern army which seeks the development and distribution of those utilities at lowest cost for the primary good of the great mass of the people who must have them if they are to maintain the standards of their neighbors and of the civilization of today."
(Governor Roosevelt, November, 1930.)

"Back of the utilities in their attack on our American form of government is the whole fabric of political corruption, the underworld, the protected racketeer and criminals of high and low degree."
(Governor Pinchot, inaugural address.)

"Two forces are struggling for the control of the government of the United States. One operates under cover. Its central purpose is to control the government and so prevent it from protecting the people against manifold extortions which take unjustly from the breadwinners many hundreds if not thousands of millions of dollars each year."
(Governor Pinchot, inaugural address.)

"The power interests are mulcting the American people of at least $750,000,000 a year in excess charges."
(Letter from People's Lobby; Professor John Dewey, president, to President Hoover, November, 1930.)

The Utilities Are in the Court of Public Opinion—Not in a Court of Law

"THE utilities are not in a court of law, at all, but in a court of public opinion, where fanaticism, oratorical intemperance, and political nonsense have the same familiarity and propriety as the tarlatan skirts of a lady bareback rider in a circus, and are just as transparent."

THERE is, of course, a great deal more of this, some of it probably worse. I have simply dipped blindly into the barrel and come up with a small handful. Governor Pinchot does not quite achieve but he closely approaches the perfection planned for him by the scalawags of utility publicity offices in the plot hereinbefore outlined. A little more fervor, a few more cuss-words, and he will have "arrived." The stuff in his inaugural was pretty good, particularly the stuff about the underworld tie-in with the utilities. How much better he is than Governor Roosevelt can be seen from a comparison of the latter's statement made in November, 1930, with Pinchot's inaugural, in January, 1931. Roosevelt conceived the idea of a "war" and "two armies," and two months later Pinchot took the same idea and breathed fire into it. There is the same difference between these two men in the handling of this theme as there is between Bishop Manning and Billy Sunday.

THE fact is, all the shouters on both sides are overloaded with parcels of antiquated notions about the mental processes of the common citizen. They are still living in the days of Francis Bacon who discovered, in his *Novum Organum*, that "the human understanding, when any proposition has been once laid down (either from general admission and belief, or from the pleasure it affords), forces everything else to add fresh support and confirmation: and although most cogent and abundant instances may exist to the contrary, yet either does not observe or despises them, or it gets rid of and rejects them by some distinction."

This simply means it can be written down as philosophic dogma, that "if you call a man a crook often enough people will finally begin to believe it is true." (Here, indeed, I quote from a utility leader, an enemy of the "sin of silence," and obviously a student of the Baconian philosophy.)

I think holders of these notions forget two things. One is that the violence, persistence, and overwhelming bulk of propaganda in modern times have completely upset the Baconian theory. Instead of adding "fresh support and confirmation" to some proposition, additional propaganda nowadays frequently merely adds

fresh nausea. Propaganda was new in Bacon's time and he was explaining it and its effect on morals and politics. All learning, all information was inaccessible. Bacon's world was just coming blindly out of a thousand years of intellectual darkness.

Today all learning is accessible. There is no excuse for anyone's being ignorant of anything, unless he be half-witted. Mankind pushes back the frontiers of knowledge all about him; and one of the things of which mankind has acquired the most knowledge, especially in America, is the tendency of his fellows to demand his attention and his support by means of printed, spoken, written, radioed, and electric-lighted words. Fed on propaganda almost from the days of his first bottle, he no longer, as in Bacon's day, ignores and despises facts or "gets rid of them and rejects them by some distinction." Adrift in a storm of high-powered hooey, he hugs an honest fact to his bosom like an archaeologist hugging a rare prehistoric fibula.

MONTH after month the utilities turn over to the modern public a flood of honest facts, in the light of which the ballyhoo of the dragon-slayers sounds silly; in the light of which, indeed, the reams of "innocence copy" from the bejeweled offices of the utility publicists sound almost as futile. These facts consist of monthly bills for light, heat, and power so ridiculously low for a service so consistently painstaking and valuable that the roars of outraged redeemers produce the embarrassment we feel for a farmer at a melodrama who jumps to his feet in the gallery and dares the stage villain to mistreat our Nell.

We feel that we here represent the calm and considered view of old John Quincy Public. Can it be that old John Quincy has not sized up the ridiculous situation—that this sovereign American citizen who sees through all our nationally famous stuffed shirts, and eventually comes to sound conclusions about everything American from Big Bill Thompson to Aimee Semple McPherson, will be hoodwinked at last by these simulated furies over the size of his gas and electric bills?

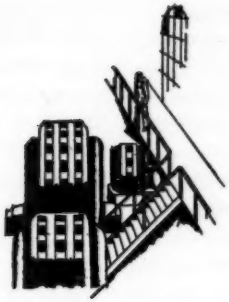
I strongly doubt it.

Certainly John is sufficiently familiar with his own burdens to know which galls him most, and of all his crosses of sorrow, including his rent, food, education, clothes, and liquor, he knows his gas and light bill is the least. So that trying to get him interested in improving his lot by a holy war to reduce his gas and light bill, is like advising a man with arthritis, stomach ulcers, gall stones, cirrhosis of the liver, and baldness, that the way to begin restoring his health is to use a good hair tonic.

WE feel that we express the hope of all sober citizens when we pray for the success of the horrid plot here for the first time fearlessly unmasked, since it is designed to accomplish two needed reforms in this country:

(a) The gagging of the ballyhoo artists of the Anti-Power Trust movement and:

(b) The gagging of the ballyhoo artists of the public utility industry.



Who Should Pay the Cost of Rural Extensions?

Why the ratepayer should share the burden with the utility

In the preceding number of PUBLIC UTILITIES FORTNIGHTLY Dr. Albert Levitt of Redding, Connecticut, presented his reasons for maintaining that the burden of cost rests upon the utility corporation, and he outlined his controversy on this point with the public utilities commission of Connecticut and with the superior court of that state; a ruling on "the Levitt case" from the supreme court of errors is now pending. The author of the following reply to Dr. Levitt was formerly electrical engineer of the Connecticut commission and associate professor of electrical engineering at Yale University.

BY ARCHER E. KNOWLTON

EVERYONE has heard the remark of the proud mother watching her son on parade for his first time with the troops: "They all seem to be out of step but John."

Anyone who asserts that the utilities should be required to make hopelessly unprofitable line extensions more or less promiscuously is pretty much out of step with all court and commission rulings on this point.

I do not mean to say that the argument advanced in such a contention will never be the ruling principle of regulation or even the maxim of the utilities themselves; the left foot may even be called the right foot some day. Stranger revolutions than that are happening before our eyes while capitalism is assimilating socialistic practices in the very effort to perpetuate its beneficences in the face of antagonistic influences. But the whole concept of regulation on the basis of fair return on investment will have to undergo reversal before wholesale extension of service to reach all sparse territories can be required.

OF course, the full application of the proposed *criteria* of service extension can mean no less than universal service. All unserved persons could invoke the proposed concept with complete impunity. Whatever rights are granted to the Mr. X, specified in Dr. Albert Levitt's article,[1]

[1] See PUBLIC UTILITIES FORTNIGHTLY, April 28, 1932.

could be asked by all the other X's; in that case X would cease to be an unknown quantity. The only factor that would deter them from demanding service would be the expenditure they would have to make in equipping their homes for electric service.

Before proceeding with the main theme, it might be well, however, to answer specifically six of the assertions made in Dr. Levitt's article.

1. The electric utilities do not insist, nor do the commissions rule, that every extension should pay for itself from the beginning.

(Most of the extensions made, even those made without pressure by the commission, are unprofitable at the outset. Fond hope and favorable experience support the expectation that they will contribute their share to a fair return after a few years.)

2. Any contribution made by the prospective patron toward the cost of building an otherwise unprofitable extension is not a gift to the utility corporation.

(Title to the property built with the money usually reposes in the company, it is true, and it is usually permitted to include its value on appraisal. But the patron has not contributed the property: he has merely advanced funds which reduce the company's outlay to a reasonable expectancy of profitableness. The common practice of refunding the advance as other new customers enhance the revenue renders that advance more a loan than a gift.)

3. There is speciousness in the argument that a particular extension agreement's call for an annual revenue of $288 represented a flat gift of $168 per year forever to the company just because the estimated consumption would bring $120 at the rate applicable in the nearby territory already served.

(The figure of $120 is no index of the cost or value of the kilowatt hours delivered to Mr. X a distance of —— miles from compactly settled territory in which the prevailing rate applies.)

4. The claim that the utility company might at the moment be making more than a fair return is irrelevant.

(If the existing return should prove to be too high then existing customers should benefit by a reduction in rates and not be forced to make an involuntary contribution in order to make service to Mr. X possible. Any other view would entail conscription of property and inject the very rate discrimination which statutes make a prime objective of regulation.)

5. Of course, the loss suffered by unprofitable extensions would have an effect on the earnings of the company and it would admittedly be imperceptible in the case of a large company making a single extension.

(It would not necessarily be imperceptible, however, in the case of a small local utility or even with a large one if the prevalence of the proposed principles should act to multiply the applications for unprofitable extensions.)

6. "At the present time," states Dr. Levitt, "it would pay the light and power companies to extend their lines into even the most sparsely settled districts because the energy which is now lost and wasted could be sold at rates which would bring more than a reasonable return to the companies."

(PUBLIC UTILITIES FORTNIGHTLY is not a technical journal and consequently is not the place in which to argue about resistance losses in conductors, unavoidable hysteresis and eddy current wastes in transformer cores and 24-hour efficiencies. But back in my professional days at Yale I was prone to flunk students who had any such grotesque misconceptions of electrical technology as that quoted. The justification for such academic rigidity would probably have been found in their discomfiture when faced in rejoinder with this question: "If losses now incurred on Main street could tomorrow be turned to profitable sale on Haystack road, then why is there not equal incentive to turn them to profitable use today on Main street itself?")

UNDERLYING all the ramifications of the extension problem there seem to be just three fundamental issues involved in Dr. Levitt's contentions:

First: How far does the criterion of reasonableness of return extend into the successively smaller subdivisions of utility property?

Second: Can city patrons be required to underwrite the cost of serving sparsely settled districts without creating a large element of discrimination?

Third: Does the possession of a charter imply the relentless obligation to serve the entire territory stipulated in that charter?

STATISTICS are not available for a precise determination of the cost of service extensions to all unserved homes in Connecticut. Nor can the prospective revenue be set down with any high degree of accuracy. Reasonable assumptions can, however, be made and if these result in a large discrepancy between cost and revenue then some of the large difference can be spared to modify the assumptions to suit anyone's tastes.

Connecticut electric utilities have some 360,000 residential customers. Their total book value of plant is around $154,000,000 and the total net corporate income is about $14,700,000. There are probably 14,000 homes largely located on the unmetalled highways, which are not now reached by electric service. Their customer-per-mile density will run low—let us say one for every five sevenths of a mile. Each mile of line extension will cost approximately $1,400 and, therefore, to reach each unserved home will entail a capital outlay of $1,000. This is exclusive of transformers, services, and meters which can safely be put at another $65 per customer.

Here then we have a commitment of $1,065 per customer, or $14,910,000 to bring electricity within the doors of 14,000 of them.

PRODUCTION expense would depend on the kilowatt-hour consumption, the load factor, and the demand characteristics of the typical user. A figure of $9.50 per customer would be representative for an assumed average use of 840 kilowatt hours per year to cover the plant operating and capacity charges. The maintenance cost on distribution system, at 3 per cent would be $31.95; depreciation would account for another 3 per cent or $31.95. Commercial expense of $2.75 along with general expense and taxes of $13.85 would create, in conjunction with the aforementioned items, a total cost to serve of $90 per

¶ "WHERE *there is a reasonable prospect of future development, less than a minimum reasonable return may and in most cases should warrant the company in making the extension, but a utility is not required to spend its resources for a prospective building development, unless the property owners themselves coöperate in a material way.*"

—CONNECTICUT PUBLIC UTILITIES COMMISSION

year per customer, exclusive of any return on the distribution investment. If the latter is taken at 7 per cent, or say $75, then the real total annual cost for an 840 kilowatt-hour customer is $165.

The 840 kilowatt hours at prevailing rates will bring in a revenue of about $60 per customer per year. There is then a dead loss of $105 per customer which places the transaction in the realm of philanthropy and not in the realm of business.

Putting it in terms of the aggregate transaction, a capital outlay of $14,910,000 would bring in a revenue of $840,000. This gross take-in in itself is less than 6 per cent of the investment. But when one acknowledges $1,260,000 of inescapable operating charges it is evident that out-of-pocket costs will exceed receipts by $420,000. When loss of return, at 7 per cent, is included, the whole extension enterprise will have occasioned a $1,463,700 loss on a $14,910,000 investment.

Some engineers believe they can build rural lines safely and durably for as low as $500 per mile. It is, of course, doubtful whether the quality of service derivable from such lines would approach that from a $1,400 per mile construction or even be wholly adequate for farm service. Cow-milking, egg-hatching, chicken-brooding, and food refrigeration brook no desultory service. Continuity is even more important than in urban usage. But even admitting the acceptability of such cheap rural construction, the carrying charges on five sevenths of a mile of it, with transformers and meters, would represent a cost-to-serve of $120 when added to the $90 already taken to cover everything but interest on investment in distribution system. The $60 annual revenue from our assumed 840 kilowatt-hour per year customer would leave in this case a shortage of $60; $30 of this would be out-of-pocket loss on operation, and $30 a lost interest recovery. Here the wholesale experiment would entail a loss of $840,000 per year on a $5,910,000 investment, something to be offset by overtaxing existing customers.

Cheap rural construction is an answer to the border-line case but it is no cure-all for the ills of unserved territory of large expanse.

Current practice of making individual extensions if they show any prospect of early balance of receipts and cost to serve is the industry's partial and progressive answer to the situation. The utilities, even in little Connecticut with its short distances, high population density, and predominating industry, could not safely undertake such an enterprise as has been proposed. They could not with economic justification do more than resort to attritional methods in converting the heathen beyond the borders of electrical civilization. Also, the city brethren are not yet won to the gospel of universal brotherhood to the extent that they are willing to have their electrical dollars support the sending of copper-and-wood missionaries into stolid and unenlightened territory.

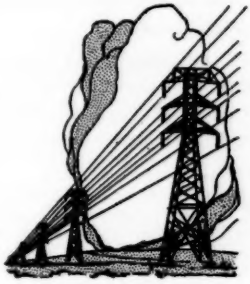
Recognition of these factors is infused into a wide range of commission and court rulings. The case which precipitated this bifurcated dis-

The Three Fundamental Issues of the Rural Extension Problem:

"FIRST: *How far does the criterion of reasonableness of return extend into the successively smaller subdivisions of utility property?*

"SECOND: *Can city patrons be required to underwrite the cost of serving sparsely settled districts without creating a large element of discrimination?*

"THIRD: *Does the possession of a charter imply the relentless obligation to serve the entire territory stipulated in that charter?"*



cussion of service extension policy was a Connecticut case. The commission's decision, adverse to the petitioner, reiterated what had been said in several similar electrical extension cases. It also showed a high degree of concordance with rulings in kindred cases in other states. For that reason a few of the significant pronouncements of the Connecticut commission are reproduced here as an adequate index of the nation-wide thinking in regulatory circles.

IN 1913 an adverse decision on Root's application for extension of gas service by the New Britain Gas Light Company, was appealed. The supreme court in 1916 (91 Conn. 134, P.U.R.1917C, 102) said this about reasonableness of return:

"The relevant facts with which the appeal and finding and order appealed from most concern themselves, relate to the cost of the extension, estimated at $20,000; and the incommensurate prospective present return thereon. These are by no means the only considerations which should enter into a decision as to the propriety of the company's action. Of course, a public service corporation should not, save possibly under some exceptional circumstances not present here, be required to give an enlarged service at a considerable cost where the prospects of return for many years to come are so meager as to be out of all proportion to that cost. But it is equally true that its duty in the exercise of rights that are essentially monopolistic in their character will not always permit it to stand by and withhold a desired service within its territory until such time as that particular service promises an adequate return from its inception.

"The question of a public service corporation's duty is not one which is determinable by the application of any such simple test as 'Will the proposed new service be immediately self-supporting or remunerative?' Its duty is measured by what it ought reasonably to be called upon to do. The test sets up reasonableness as the standard, and in its application here as elsewhere it takes into account all relevant circumstances and has no definite or precise measure. It is clear, however, that in a case like the one before us, prospective future returns from the new undertaking is a factor not to be overlooked or passed over slightingly."

OCCASIONALLY these cases arise in connection with real estate promotion and prospective building developments. The Connecticut commission had this to say about such situations in Docket 5563 (1930)

Stanley *v.* Danbury & Bethel Gas & Electric Company, where it appeared that a revenue of $108 per year would follow a $2,205 investment in 6,200 feet of pole line to serve a single prospective user:

> "Electricity is a rapidly developing utility and its use is becoming more and more in demand, even in rural sections, for general household purposes. In keeping with this development and demand, electric utilities should adopt liberal policies pertaining to the extension of service into new and rural territory. Where there is a reasonable prospect of future development, less than a minimum reasonable return may and in most cases should warrant the company in making the extension, but a utility is not required to spend its resources for a prospective building development, unless the property owners themselves coöperate in a material way and give substantial assurance that the prospective development will ultimately become a reality."

THIS same case, in which, incidentally, Dr. Levitt was attorney for the petitioners, brought out the following comment by the commission on the matter of the charter obligation:

> "The mere fact that the utility company's charter includes certain remote and undeveloped territory does not necessarily mean or imply that the company must extend its service into such territory upon demand of one or a limited number of prospective patrons. The utility company's franchise obligations require it to supply service at reasonable and nondiscriminatory rates to all parties demanding service within its chartered territory, if this can be done without violating certain well-established legal and economic principles. The principles involved in the question as to whether an electric extension should be ordered into new and undeveloped territory located within the chartered territory of the utility are primarily the length and cost of the extension, probable gross revenue and operating expenses as determining what, if any, return on the capital investment will accrue, the prospective future development of the territory with such utility service available and in general the number of people to be served as affecting public convenience and necessity. The reasonableness of the company's rates in a territory already being served is not a controlling factor in determining the reasonableness of a particular extension. If the rates are too high, resulting in unreasonable profit for the company and imposing an undue burden upon existing ratepayers, then the rates should be reduced to a reasonable rate for such service, rather than continue the ratepayers' burden for the benefit of unprofitable business and injecting into the rate structure unwarranted discrimination. Moreover, the continuance over a reasonable period of time of a policy of extensions into unprofitable territory without regard to the cost of the service may reasonably be expected to tax the financial soundness of even the strongest companies and result not only in inability of a company to earn an adequate return upon its property as a whole, to which it is lawfully entitled, but also may reasonably be expected to deprive the company of credit and of the means of raising capital with which to carry on its public service. Such a policy is, therefore, economically unsound and dangerous as striking at the very heart of a utility company's obligation to the public."

OTHER quotations bear on this joint question of charter obligation and reasonableness of return:

> "When a charter is granted a public service company, and the company operates under the privileges granted by the charter it seems reasonable to demand that it furnish service in parts of its territory which may be of less than average remunerativeness as well as in territory which may yield it an exceptional profit. By virtue of its charter it precludes from the field any other company which might be willing to furnish the desired service in that part of its territory which for itself is less profitable or not profitable at all. Within certain limits, therefore, the commission feels that it is equitable to require such a company to extend its service into territory which promises but small return and it is within its judgment to define what limits are equitable in any particular case. It does not follow, however, that a public service company should be required to extend its lines and supply service, at a very large expense in proportion to the income received for such service, to every inhabitant located within its chartered territory."[2]
>
> "Where the extension of an existing line, if made only for a short distance, could supply the service at a cost not disproportionate to the probable return, the demand for making such an extension

[2] Stoddard *v.* United Illuminating Co. (1914) Docket 1126.

would obviously be a reasonable one and one which could be reasonably met; on the other hand, it can hardly be claimed that the utility is under a duty to extend its service at its own expense on the demand of a group of inhabitants residing at a long distance from a point to which its line is already extended, where the rates to be charged for the service would but to a slight extent compensate the utility for the expenditure involved; in fact, without any certainty that there would be a continuous use of the service even after it was brought to them. . . .

"Inasmuch as the facts show that no development may be expected within this territory, the commission believes this is an additional reason for deciding that it would not be justified in ordering the extension. To hold that the utility should extend its line whenever requested to do so, to any part of its chartered territory, no matter how sparsely settled, would render it impracticable and might make it impossible for the utility to serve the rest of the community at a fair rate, or even to exist. Indeed, the cost of an unreasonable extension would add an unfair proportion to the cost of service in sections where service would otherwise be profitable, at a fair rate." [3]

"The commission desires, wherever it is possible to do so, with justice to both sides, to encourage the extension of electric service into rural territory recognizing its advantages to the inhabitants; but it cannot legally order a utility to extend its service where the revenue will probably not even pay all the operating expenses and overhead charges apportionable to the line, and not afford any return on the cost of the extension to the utility. The fact that the utility made an extension at a loss, expecting to obtain power consumers to make it pay, is no criterion for the commission in passing upon, as in this case, whether or not the usual rates should be charged for an extension of this kind." [4]

HERE in unmistakable terms is the precept that a charter does no more than imply that service shall be extended throughout the allotted territory. It does not even imply that the extensions shall occur as fast as receipts become reasonably commensurate with costs to serve. And if it did such a stipulation of reasonable balance of income and outlay would presuppose an early likelihood of profitable experience with the extension but not necessarily an immediately adequate return. Both these points are left to discretionary treatment by the commissions under the rule of reason as befitting the circumstances of each case.

Not being versed in the law, I can only express an individual layman's conception of a charter. To me it means a permissive document and not a mandatory one. It partakes more of the nature of a patronizing grant than of a repressive edict. The expectation that the charter rights will be exercised is present in tacit form; if they are not exercised they can be annulled or vitiated by the grant of overlapping rights to a more active second party. A utility is a private corporation given by the state the right to engage in a kind of business which is special because it more intimately affects the interests of the state and the patrons, collectively and individually, than does the activity of the ordinary corporate enterprise. The institution of regulation has not supplanted the intent of the charter-

[3] Sadikoff *v.* Danbury & Bethel Gas & E. Co. (1922) P.U.R.1923A, 319.

[4] Howard *v.* Putnam Light & P. Co. (1924) P.U.R.1925B, 515.

¶ "DRASTIC *curtailment of that utility profit or conscription of capital to make rural service electrically complete in one quick operation would stifle the benefits which 70 per cent or more of the population are deriving for the sake of extending them to the remaining 30 per cent or less.*"

ing concept. In fact, it confirms that intent by imposing supervision over rates, securities, and service in reciprocation for the monopoly and profitable privileges granted by the charter.

SUCH a commonly accepted view of the charter has grown out of centuries of history made by kings and parliaments. If the charter concept had acquired the proposed mandatory attributes before telephone, gas, tramway, and electricity inventions ripened for commercial exploitation, it is doubtful whether any individual or corporation would have had the courage to engage in such enterprises. The motive of profit and compensation is the stimulant of all business.

Electric service is still predominantly a private enterprise built on the profit motive but in full awareness of the fact that magnitude of profit is limited by the agency which made that profit possible by restraining uneconomical competition. Drastic curtailment of that profit or conscription of capital to make rural service electrically complete in one quick operation would stifle the benefits which 70 per cent or more of the population are deriving for the sake of extending them to the remaining 30 per cent or less. If, as, and when the present beneficiaries of electric service in the most densely populated sections are willing to socialize the enterprise and make sacrifices to subsidize the rendition of service to every hamlet, then commissions and courts may be expected to look favorably on all petitions for extension of electric power lines.

THERE are ample reasons why telephone service usually reaches beyond the boundaries of the electric distribution system. There are ample reasons why gas and water supply systems do not reach in general as far as the power wires. But in the main, the regulatory attitude and the determining economics are the same for this whole group of household services. It is simply that each extension shall offer reasonable prospect that the revenue which it produces shall before too long carry its share of the system investment. In the meantime the proprietors of the electric business are voluntarily conforming to the objective set up as a peremptory demand by Mr. Levitt—extending service faster than is strictly profitable, knowing full well that there are few backsliders among customers and that most of them wax more enthusiastic as their appreciation becomes aroused.

Ultimately the electrical map will look like the physiologist's drawing of the human nervous system in which no pin prick is possible without running afoul of a nerve. How soon that time will be reached will depend on the rate of evolution of the situation in its present channels and not on the prospect of inverting the concept of the charter, abandoning the principles of incremental profitableness, and applying a platform of conscription and subsidy to semi-public enterprises.

ON only one ground could the proposed program possibly be substantiated. It is that electric service has completely outgrown the attributes of a luxury and a convenience

and has become such an item of necessity that it should be rendered as universally accessible as the mail service, for example. But even there the government does not send its rural carriers up every little lane and by-road. Clusters of mail boxes are mute testimony that even profligate Uncle Sam must say, "If you want it you will have to come and get it."

Distance lends enchantment but rural distances have their drawbacks too. The little red schoolhouse, the village store, the doctor, and even the filling station do not lie as close to the rural dwelling as to the habitations of the city folks. Those are real necessities transcending the service value of electrical energy and this remark in no way disparages the claims made for the value of having electricity under finger-tip control.

PERHAPS all the questions about extensions can be simmered down to one:

"Shall a considerable share of the marginal profits of utility operations be devoted to progressive extension into all contiguous territory as fast as it reveals any prospect of profitable return on investment?"

The answer to that is unmistakably:

"Yes."

If it were not "yes" no one could account for the phenomenal spread of electric service in the last decade or two throughout the entire country. And being "yes," it means that a large part of the unserved territory will have been served long before courts and commissions concede that they have been "out of step with John" during all of these years.

Oddities About the Carriers

No Pope has ridden in a railroad train since 1870.

* *

A SPECIAL car, equipped for dancing by passengers, has been put into service by the Delaware, Lackawanna and Western Railroad.

* *

A LOCOMOTIVE known as *"Smoky Mary"* was recently consigned to the scrap heap in Louisiana after service on a 4½ mile railway dating back to 1830.

* *

IN order to improve a city neighborhood in which it operates, a district railroad has erected a handsome five-story house front in Bayswater, England, to mask its right of way.

* *

A RAILROAD in New York has been sued by a 72-year old woman who claims that due to an accident for which she holds the road responsible she can no longer indulge in "skating, bob-sledding, and dancing."

* *

THE "punctuality record" is claimed by the *National Limited* train of the Baltimore and Ohio Railroad; it has covered 4,250,000 miles in seven years of service between St. Louis and Washington, with a punctuality score of 97 per cent.

A ROUND TABLE CONFERENCE DISCUSSES THE

Liberal Viewpoint on Regulation

A summary of its conclusions and an estimate of its significance, as seen by one who took part in its deliberations—

WILLIAM Z. RIPLEY

THE recent Round Table Conference on Public Utility Regulation held in New York is highly significant for several reasons.

It brought together a considerable company of disinterested, public-spirited persons, concerned in and about the welfare of one of the newest of the most important industries in the country. During its deliberations it included a chosen few members of regulatory commissions; these were selected partly because their administrative bodies had real power, partly because those in charge of them were notably intelligent, public spirited, and fearless. No public utility men, least of all glad-hand entertainers, who function too largely at gatherings like these, were present; nor were they desired. The only reason, I assume, why responsible and straightforward executives were not invited, was because the time was too limited to permit other business than an attempt among those whose point of view was more or less identical, to discover their differences; and to inform themselves intelligently as to what the public had a right to expect in the way of honest management, reasonable rates, and adequate service.

Personally, I would have preferred to admit a few of the best types of leaders of the great companies. There was no fear whatsoever of any so-called "secrets" leaking out. It was purely a question of the time at command, and of the necessity of taking counsel one with another among a group of intellectual affinities, so to speak.

THE next step in an orderly analysis of the situation, once these self-constituted spokesmen of the public interest know where they stand basically, should be that contact should be established with the men in the business. No solution could be possible until such men were consulted, were asked to advise, and particularly were relied upon to indicate shortcomings or weaknesses in any proposed program. Speaking purely for myself, I cannot overemphasize the statement that the exclusive one-sidedness of this particular company was not due to any desire for Star Chamber proceedings. Everything

was open and above board. The only thing which was begrudged was time for shaping up this first stage of what many of us hope will be a continued progress toward better understanding all along the line.

THE press notices gave an unmerited impression of conflict within this carefully selected group. This was particularly the case in connection with the attempt to formulate a program, or to effect a statement of policy. Outwardly it looked as if, to cite a newspaper headline, these would-be utility reformers had "split."

This is an absolutely unwarranted impression. There were considerable differences of opinion, but these had to do with particular steps in procedure rather than with essential underlying issues. There was agreement unanimously, for example, in the forthright and fearless pronouncement of Professor Bonbright as to the misuse and collapse of the holding company. Who could doubt that after what has since happened at Chicago, for example? On the four points which he made there really was not room for the slightest divergence of opinion.

THE two most widely attended round tables were those dealing with the holding company and with Federal regulation.

In this latter field, I think I am stating it conservatively, that there was agreement that inasmuch as there were certain matters which were well beyond the power of the individual states to handle, the Federal government must intervene, and that too in the near future. As to details concerning the exact allocation between state and Federal jurisdiction, there was not time to deal with it. But as for the field of publicity of accounts, of financial regulation of interstate holding companies, and, of course, for those services and charges which were distinctly interstate, unanimity prevailed. There was, of course, hesitancy among the state commissioners lest supersession of state regulation by the Federal government should take place. Speaking again for myself, the primary purpose of the conference on this topic seemed to be to canvass the situation carefully, in order to discover upon what basis this division between the several states and the nation should be effected. Substantial clarification, I think, resulted from this deliberation. The nature of the work to be done in the future, at all events, was clearly outlined.

AND now for this apparent "split," which may perhaps have given unwarranted satisfaction to those who would prefer to let everything alone for the future.

This "split" came in the concluding session, when everybody suddenly realized that the task of formulating conclusions was far greater than the available time at command made possible. There was also difference of opinion as to the desirability of issuance of any statement of policy at all. By inadvertence, because the whole affair was most intimate and informal, notice had been given that there would be such a statement. A committee did very hastily frame a statement which was submitted to the conference in the closing hours. One group pinned its faith to this docu-

"Inasmuch as scientific standardization and publicity of accounts both for operating and holding companies, together with assurance of access to all files and papers, is a condition precedent to any attempt to regulate rates, to assure adequate service, or to protect the investing public, such supervision of accounts should underlie any regulatory plan, either state or Federal. This will entail revision of the present uniform classification of accounts to serve as a guide in establishing the equities of the various rates as well as of total earnings."

"Had this conference done nothing else than to place such a paragraph foremost in its rough draft of a program, all the effort would have been worth while."

ment, as evidence of definite fruit of our deliberations. The other — including myself—was of the opinion that the refreshment of our spirits, clarification of our aims, appreciation of our specific limitations, and a closer acquaintance one with another, as the beginning of a permanent organization, was the really rich reward which had already been gleaned. We felt that no declaration, and particularly a hastily contrived one, which could not aspire to embody the varying shades of minor difference between us, was politic at this time. The outcome was again agreement. For the one party rested with mere submission of a proposed statement, which was not even discussed in any detail. The other group acquiesced in informal issuance of this rough draft in deference to their associates. Thus we parted amicably—again I speak for myself—grateful to those who had really initiated the whole affair.

WHY, then, did I issue a specific disclaimer of responsibility in the formulation of this rough draft of a program? It was partly because of a feeling that the situation did not call for quite so indiscriminate a condemnation of the management of the industry as a whole. The force of this contention, which had in mind, later on, coöperation and consultation with the men in the business, was acknowledged as just. But there was no time to effect such modification of the statement before adjournment. It seemed best, therefore, to let it stand, but as a mitigation of its overstatement, I felt it to be in the interest of future coöperation to personally qualify this too sweeping assertion of abuse and failure.

The state commissioners also declined to join in consideration of this declared policy or program. That, too, was as it should be. They bore official responsibility which we others did not; and in any event, even after the most detailed consideration, they must make sure of any specific commitment which might prejudice them later on in the performance of their duties. And so they refrained as a body. And those of us who were "resolution-shy," found solace in this circumstance; because it afforded yet another reason for holding back our horses until they were really properly

trained and thoroughly fit for the race.

THERE was one paragraph, however, in this incipient statement of policy which appeared to be acceptable to a large majority of those present. It was, as a matter of fact, the only plank in the platform with which I had anything personally to do. Substantial agreement as to its importance is afforded by the fact that before this announcement of policy was even presented, this paragraph was insinuated ahead of everything else as a recommendation. To my thinking, it constituted the corner stone of any sound regulation, state or Federal. For that reason it deserved priority among recommendations; and I am confident that in the field of political action its adoption should be the first step in any reform. The recommendation is as follows:

> "Inasmuch as scientific standardization and publicity of accounts both for operating and holding companies, together with assurance of access to all files and papers, is a condition precedent to any attempt to regulate rates, to assure adequate service, or to protect the investing public, such supervision of accounts should underlie any regulatory plan, either state or Federal.
>
> "This will entail revision of the present uniform classification of accounts to serve as a guide in establishing the equities of the various rates as well as of total earnings."

HAD this conference done nothing else than to place such a paragraph foremost in its rough draft of a program, all the effort would have been worth while. For it would serve notice that the widespread preoccupation, heretofore, with reasonableness of rates and of valuation deals merely with symptoms and not with remedies. The basic remedy must be complete publicity as to the cost of unit production. Such data must be rendered comparable through the enforcement of such a standardization of accounts as is prescribed by the Interstate Commerce Commission for railroads, the telephone, and the telegraph. Anything short of this deprives both regulative authority and the industry itself of the best scientific test of efficiency of operation and of honest management. Such publicity operates to protect both the public as consumer and the multitude of people whose capital is invested in the business. More bull's eyes are hit by sure aim with this weapon than by resort to any other implement.

This experience with practically unanimous adoption of a plank in a proposed platform provokes the opinion that, had time permitted, careful and precise wording of a number of other subsequent planks would have resulted successfully. But even without the shift of this proposal to first place, almost without debate, I should have felt that what appeared like conviction among us as to this matter, in entire absence of any proposed resolution, would have been well worth while.

BROADLY viewed, this experience brings into strong relief the imperative necessity of such conferences among those who are like minded, in order that they may agree upon what it is reasonable and politic to advocate in future. The first thing which happens in any such gathering is that it assorts itself, like sand or gravel shaken up in water, into distinct strata. A right and a left wing discovers itself. One group would go much farther than another. This contingency was in a measure abated

in this conference, however, because all consideration of government ownership was barred out. This was a council upon government regulation, quite apart from any other policy. Such graduation as developed, however, did not differ so very much in degree. There are about so many compartments, so to speak, into which regulation may be sorted. These are, respectively, rates, service, accounts, finance, and security issues. We seemed to be agreed that all of these were important and interdependent. How they should be divided up between the Federal government and the states was merely a matter of detail.

WHAT, then, we seemed to be at variance about, was really of secondary importance. For it had to do with the manner in which these objectives could best be obtained; the path, as a matter of policy, which would most directly lead to the top. Some would fight with a shillalah; some with a rapier; some would prefer persuasion, and even coöperative endeavor. I, for example, look to substantial progress, through enlistment of the true and responsible leaders of the business, to the end that it be policed in the interest of sound development and established credit. Others, like disciples of Governor Pinchot, perhaps, would swing the big stick. So again, some would fulminate with resolutions. Some crave publicity and rush into the press. Others, like Commissioner Maltbie, deplore "the American habit of passing resolutions."

Actually, progress will result from resort to a blend of all these policies. But, because upon such detail there was divergence of view, not possible to be ironed out within a brief space of time, there should be no misconception upon the main conclusion.

The public utilities of today are just as surely bound to be strictly held to an accountability to the public and to their owners in the immediate future, as were the banks, the railroads, the telephones, and the telegraph companies in the years which have passed.

Utility Items of Passing Interest:

To aid color-blind motorists to observe street traffic signals, one city is about to experiment with lamps that vary in shape as well as in color.

* *

THE municipality of Muscle Shoals, Alabama—located near the world-famous Wilson Dam power plant—does not boast a single electric light.

* *

A MAGPIE, with a small steel trap clamped to its leg, lit on a telephone wire in Baker, Oregon, and caused a short circuit that paralyzed long-distance service.

* *

THE only railroad line in the United States which has maintained its stations on the left instead of on the right side of the track is the Chicago North Western line.

* *

THE handset "French telephone," made familiar to Americans in motion pictures with European settings, is not French at all; it was patented by Alexander G. Bell and used in the United States as early as 1878.

OUT OF THE MAIL BAG

"Going Value"; Its Importance in Utility Rate Making

IN a recent article in PUBLIC UTILITIES FORTNIGHTLY,[1] Luther R. Nash devoted several pages to a critical analysis of my views on going value as expressed in the FORTNIGHTLY of November 12, 1931. It occurs to me that the time is ripe to run this problem of going value to the ground; to see whether through direct expression of conflicting opinion this issue may not be narrowed and more sharply defined, and whether by disspelling confusion we may not come to agree, substantially, on the policy best to be followed in achieving the result which, I am confident, both Mr. Nash and I wish to reach. To this end I am submitting a series of comments based upon propositions set forth in his article.

1. I cannot accept the proposition that going value is of minor importance to the average consumer since the "conventional allowance of 10 per cent" means only a fraction of a cent a day to the consumer, although it may well be the deciding factor in so establishing the credit of the utility as to enable it to render adequate instead of restricted and unreliable service. In the first place, I object to the characterization of 10 per cent as the "conventional *allowance*"; "conventional *claim*" is more nearly accurate, I believe. Secondly, if these earnings and credit really determine whether adequate service can be rendered, they need not depend for their justification upon the loose argument that, after all, the allowance does not injure the individual consumer seriously. The argument suggests that as long as the "indignation point" is not reached it is proper to raise rates a cent here and a cent there to establish the credit of the company, even though the allowance *per se* cannot be justified. Why not just pass a tin cup? If a going value allowance is sound, the fact that it costs the consumer something is immaterial; if such an allowance is not justifiable, it becomes no more acceptable because it costs each consumer almost nothing. Finally, even though the direct burden of a going value allowance weighs lightly upon the consumer, it is still true that effective regulation (and hence the consumer) suffers heavily from going value claims and the resulting controversies. Weeks and months spent in preparing, presenting, and considering the most ridiculous testimony and briefs—absurd theories clothed in impeccable legal, engineering, and accounting garb; "expert testimony" fees running into staggering figures; and "judgment" allowances engendering a looseness permeating the entire valuation process, and supported by opinions which shower discredit upon the whole structure of regulation; this is the toll of going value, and a major reason why it should be discarded.

2. The method supported by the present writer is characterized by Mr. Nash as "akin to amortization." I have failed to make myself clear. The method (which I can scarcely claim as my own, since it is the mechanism universally employed by private capitalistic business to meet the problem of business risk) is simply the process of weighing the chance of losses against the possibility (or "expectancy") of profits at the time the investor makes his original commitment to the enterprise. Mr. Nash speaks of "two recognized ways" of providing for early losses which investors require to induce them to enter the public utility industry rather than some other field —the "amortization" of early losses, or their "capitalization." Recognized by whom? Certainly not by commissions or courts in the case of public utilities. One will search diligently and long through *Public Utilities Reports* to find a handful of instances in which specific allowances either to capital or operation are actually and exactly made to cover early losses. And most certainly these methods are not recognized outside the field of public utilities; general business and industry do not amortize or capitalize early deficiencies in return. These deficiencies (when they appear) together with later losses (when they appear) are regarded simply as the maturing of those business risks, the presence of which constitutes the social justification for the private receipt of profit. The rate of return which public utilities are permitted to earn contains an

[1] "How Much Today's Ratepayer Should Help the Ratepayer of Tomorrow," PUBLIC UTILITIES FORTNIGHTLY, February 18, 1932.

appreciable element of profit—not a speculative amount, since utility risks are comparatively slight—above a bare interest rate. There is no reason, thus, why, in addition to being granted freedom from competition with others of their kind, utilities should be allowed to add to their valuations the amounts by which, for any reason, they may fail actually to realize full interest plus full profit from the moment operation begins.

Do the advocates of the method of capitalizing early losses realize that their theory requires, logically, that the amount of *excess* earnings—those above a bare interest rate—be subtracted from the valuation base, even to the point of reducing that base below the figure representing the direct investment of stockholders and bondholders?

3. Mr. Nash objects to my suggestion (Dr. John Bauer's, originally, I believe) that present owners who have experienced no deficiencies in income should not be permitted to earn on a rate base increased by the amount of deficits incurred by their predecessors in title. This, he says, "is clearly inconsistent with conventional business transactions," since the present owners may be presumed to have contracted for all assets, and to have paid "for an element of value representing cost which the seller has not seen fit to collect and which the courts have generally recognized as proper." However inconsistent with "conventional business transactions" my proposition may be,[2] it is certainly not inconsistent with actual transactions in the field immediately under discussion. Courts have refused almost universally to accept the "early deficit" theory; even the Wisconsin commission which has now definitely abandoned the theory never went further than merely to "consider" it in arriving at a valuation, and the Galveston decision of the United States Supreme Court in 1922 placed the theory rather definitely beyond the pale. Just what basis is there for Mr. Nash's statement that the courts have "generally" recognized it as proper; and just what kind of an investor could be supposed to have paid more for a share of utility stock because of the chance that it might some day entitle him to an increment of value, completely speculative in amount, which courts and commissions have repeatedly refused to recognize? Just how many of these investors are there, and what element of equity do their claims embrace?

4. Under Mr. Nash's proposal that later generations rather than the present should bear the burden of the cost of attaching business to the property, the utilities commission is to be condemned if during the first few years of operation (how many, by the way?) the utility fails to develop losses. Is it not eminently to be preferred that the regularly recognized costs of attaching business—expenditures for advertising, employees training, demand creation, etc.,—be charged once and for all to operation, as, indeed, they are under typical commission-prescribed accounting systems; that rates be fixed at a level calculated to be sufficiently high to cover these as well as other operating costs together with an interest and profit return on the invested capital; and if unrecompensed deficits in fact develop (as they may or may not, and for a shorter or longer period), regard them as they are universally regarded elsewhere, as hazards which business hopes and expects to avoid, but which, if incurred, are to be borne by the stockholder as the reflection both of his special contribution to the productive process and of the profit which he once expected and which he still expects to receive?

5. At one point Mr. Nash swings to a defense of including in the going value allowance advertising costs, and so forth, incurred after the beginning of operation. This would seem to involve a confusion. The allowance cannot be expanded to include these expenses and in addition the amount by which past income has failed to cover these and other expenses and a fair return. The "early loss" theory and the "expense" theory are separate and distinct. Further, the "early loss" theory does not refer to losses incurred solely because of expenditures for advertising and so on, any more than because of other operating expenditures. There must be a clear delimitation and selection of bases or theories; the utility can scarcely expect to receive an allowance for going value calculated by adding together the fantastic results reached by all the separate methods proposed for measuring the same item.

Turning to the allied contention that expenditures for advertising, attaching new business, and other items, result in increasing permanently the capital value of the enterprise, and hence in this connection differ significantly from other operating expenses, a few questions are in order. Shall we, then, take "new customer" expense out of the operating accounts, and lessen accordingly the amount to be allowed by the Commission for operating expenses? Shall we require that stockholders and bondholders contribute the capital to cover these capital costs? Shall we, in fact, issue stocks and bonds against these expenses?

It is relatively unimportant to which accounts these costs have in fact been charged in the past; further, it is unimportant

[2] In fact, I believe my proposition is *not* inconsistent with "conventional business transactions." The investor buys *assets*—expected sources of future income, and in an individual business losses *already incurred* bear no calculable relation to income which may be expected to accrue in the future.

whether they have been covered by earnings in the past—just as unimportant as whether any other expenses have been so covered. The important consideration is where these expenses *should* have been charged in view of the fact that the utility was permitted to exact rates calculated to be high enough to cover all regular operating expenses including the costs of attaching new business, and that these rates were accepted by the utility on this basis and put into effect. And neither sound accounting practice, equity, nor any more remote "policy" can operate to permit that outlay for attaching business now to be characterized as "capital" for the purpose of increasing current rates.

6. Mr. Nash attacks "amortization" of early losses (which the present writer does not support) with the statement that it "lacks any definite period over which it could logically be spread and, therefore, lacks one of the essentials of routine accounting." One might inquire how much of "routine accounting" is to be found in either (a) the proposal to charge expenditures for attaching business to capital, or (b) the proposal to charge losses to capital; and just what is the essential "definite period" which must expire before "early" losses become unsuited to capitalization.

7. Mr. Nash, arguing from the reproduction cost hypothesis, says that estimates of the reproduction cost of attaching business should be based upon actual conditions at the time business was in fact attached, rather than present conditions, because those who argue otherwise are presumably those who with respect to other items in the valuation (such as paving over mains) insist that historical conditions of construction shall be recognized; logical consistency demands that they accept the historical approach here. Even conceding that consistency requires one inconsistency to be followed by another, the argument still impresses one as something less than devastating. It is quite capable, of course, of being reversed and applied with equal validity to those utility representatives who with respect to those same physical items have always insisted that present conditions should be recognized. Further, the present writer is scarcely precluded from insisting upon the present condition approach in calculating the cost of reproducing the attached business, since for some time he has been on record[3] as opposing the reproduction cost doctrine generally, but insisting that if it be adopted it should be accepted with all of its logical, monstrous implications (including paving over mains). Most of those opposed to reproduction cost have been guilty of a tactical error in urging that the spectacularly bad features of the method be toned down; had they been willing to insist that the rule be accepted or rejected *in toto*, it would have been banished long since.

The reproduction cost theory proceeds on the assumption that the existing property is wiped out, and then replaced, identically, and the question is: How much would it cost the company to replace this property? Now, if under prevailing accounting systems and rules of rate making new business expenditures have been and will continue to be charged to operation and thus included among the operating expenses which go into and thus help to swell the amount which rates are calculated to cover, it follows that this is not a cost of reproduction which would have to be incurred by the company in any other than a formal bookkeeping sense. It has no place in the reproduction cost appraisal under any supportable theory which that appraisal may represent. And in any event, if the appraisal be built upon the basis of present conditions—as it must if reproduction cost is to have any scientific significance for rate making—it is generally conceded that the figure covering cost of reproducing attached business would be infinitesimal.

8. Let it be emphasized that the purpose of denying going value allowances is not to beat down the utilities, nor is there the slightest danger of drying up their sources of capital. Operating accounts are available to take care of new business expenditures, and the profit element in the rate of return is offered, as it is throughout the world of business generally, to induce the assumption of business risks. The effort is simply to eliminate once and for all the typical valuation spectacle of a battery of "experts" trying franctically to build up a huge "judgment" allowance by deluging the commission with the most fantastic "testimony" which the human imagination—under pressure—can conjure up. May we not make valuation more exact, more business like, more consistent with the dignity of rate making as a scientific process?

—Ben W. Lewis,
Oberlin College

[3] XXVI Michigan Law Review, 713, 722, n. 24 (May, 1928).

A Reply to Professor Lewis

In the February 18, 1932, issue of Public Utilities Fortnightly I discussed the basic principles of amortization accounting, using as one of the illustrations the subject of going value. In this illustration brief reference was made to an earlier Fortnightly article by Professor Ben W. Lewis. I have had opportunity to read a subsequent communication from Professor Lewis in which he takes exception to my discussion in so far as it related to going value, and

expresses contrary views for your publication.

I do not wish to engage in a debate on this subject, and a statement of the fundamental differences in viewpoints will make it unnecessary. Professor Lewis maintains that utilities should assume the same risks with respect to early losses or cost of establishing a successful business as other industries. I maintain that regulation undertakes to remove the speculative elements from utility operations in order that service may be rendered at minimum cost. A study of regulatory history clearly shows that the latter procedure has prevailed to an increasing extent and with growing approval. If the risk factor found in competitive business were injected into the public utility business, it would be necessary to increase the authorized rate of return to a level approaching that found in well-managed competitive business units. The resulting distributable income would be substantially higher than that now prevailing, in which the conventional allowance for going value is a factor. I repeat the term "conventional allowance" used in my earlier paper, in spite of Professor Lewis' objection to it, because a review of authoritative decisions on the subject shows it to be justified.[1]

Incidentally, the elimination of speculative risks from the utility field is one of my reasons for favoring investment as a rate base rather than the reproduction-cost method with its possibilities of wide fluctuations and heated controversies. My views on this subject are so well known (see review of my "Economics of Public Utilities" by Professor Henry E. Riggs in the March 17, 1932, PUBLIC UTILITIES FORTNIGHTLY) as to negative any contrary inferences from the casual illustrative reference thereto in my recent paper.

EARLY losses are not imaginary. Utilities cannot, either initially or ultimately, compete in far-flung markets as can a manufacturing industry, and few of them have escaped a prolonged unprofitable struggle to develop their restricted fields. If the resultant losses are not to be regarded as speculative, regulatory history discloses only the two logical specific methods of their disposition referred to in my paper. A careful reading of the quoted decision and more recent cases dealing with the subject from an equitable viewpoint clearly discloses them as "recognized ways."

If one selects the so-called capitalization method as involving minimum annual cost, it, of course, does not mean that bonds or even stock are issued against going value, but only that it becomes a part of the rate base. It is also obvious that early losses are not losses if customers have *in fact* paid for them. A charge to operating expense is not proof that they have done so. Of course, no one would contend that there should be any duplication of charges between the rate base and operating expenses as set up in a rate case.

THE decisions disclose that going value is rarely included in a rate base in the absence of corroborative testimony. The utilities would not care to make such testimony voluminous and technical were it not for the prevailing misconceptions of the subject, the repeated efforts to ignore legal precedents with resulting contention for service at less than actual cost, or an apparent ignorance of the fact that a fair allowance for going value results in minimum rates. The primary purpose of my paper, as stated therein, was to secure such rates in the interests of the customers, not only with respect to going value but also other and more important elements of cost.

It should be unnecessary further to consider the existence of such an element as going value. There has been confusion among the tribunals as to its make-up, due in part to differences in their functions or responsibilities. In spite of this, there is a significantly consistent line of decisions which distinguish a property with an established business and one which has none. The succinct comment of one judge remains unchallenged:

"The additional value is there."[2]

—L. R. NASH,
Boston, Mass.

[1] Monroe Gaslight & Fuel Co. *v.* Michigan Pub. Utilities Commission, 11 F. (2d) 319, P.U.R.1926D, 13, 20; *Re* Indianapolis Water Co. [1926] 272 U. S. 400, P.U.R.1927A, 15, 28; Brooklyn Borough Gas Co. *v.* Prendergast [1926] 16 F. (2d) 615, P.U.R.1927A, 200, 255; United Fuel Gas Co. *v.* Public Service Commission [1926] 14 F. (2d) 209, P.U.R. 1927A, 707, 723; Columbus Gas & Fuel Co. *v.* Columbus, 17 F. (2d) 630, P.U.R.1927C, 639, 649; Plainfield-Union Water Co. *v.* Public Utility Comrs. [1928] 30 F. (2d) 846, P.U.R.1929D, 3, 23.

[2] Monroe Gaslight & Fuel Co. *v.* Michigan Pub. Utilities Commission, 11 F. (2d) 319, P.U.R.1926D, 13, 20.

The Right to Regulate a Utility's Salaries and Wages

Can the public service commissions direct a corporation to reduce the compensation paid to its executives or to its laborers? The query has been raised in Congress; the answers of the courts will be given in an article in a coming issue of PUBLIC UTILITIES FORTNIGHTLY.

What Others Think

A Crusader Assails the "Power Trust"

"THE Power Fight," by Mr. Stephen Raushenbush, does not purport to be a summary of the Federal Trade Commission's findings, but in it he has touched directly or indirectly upon most of the evidence assembled against the power industry, not only by the Federal Trade Commission, but by other investigating bodies as well as noted antiutility advocates.

Unlike the authors of a number of similar volumes now current, Mr. Raushenbush is quite honest in his espousal of the cause of complete government ownership for American power service. He favors chiefly the German method of ownership by a politically controlled operating corporation, with the possible right of private capital to invest in a minority interest. He is frankly bitter in his hatred of our present private ownership of the power industry, and in his contempt for our attempts so far to regulate it. It is a fairly complete indictment. Mr. Raushenbush and his associates have done an expert job of reporting and gathering data on one side of a great controversy. And so far as he deals with simple facts, the author's statements appear quite trustworthy.

It is when he begins to argue, however, that the author shows both lack of depth and balance. For example, there is his description of how America could buy out the electrical industry at its present value and make it pay for itself in thirty years. He adopts the ingenious analogy that the power industry is a house worth at present about ten billion dollars. The rate of 7½ per cent return is what the American public now pays for rent on this house which, of course, increases in value from year to year. Now if we bought this house upon money raised on government bonds paying only 4½ per cent interest, we would save the difference or about 3 per cent which in thirty years would amount to over twenty-five billion. Mr. Raushenbush states:

> "At the end of thirty years we have paid off the mortgage and own the house. Under private ownership our rent would have been $1,500,000,000 in 1960 and $1,521,500,000 in 1961. Under our own ownership we collect the same rent in 1960, pay out $900,000,000 for the actual use of money, and put aside in savings $600,000,000. In 1961 our rent bill is 0. We are absolutely clear. From that time on to eternity we pay nothing for rent. Our children pay nothing for it. Their children pay nothing for the use of funds. We own the house free and clear."

PROBABLY the easiest way of puncturing this rosy bubble is by applying the old logical test of the scholastics—the *"reductio ad absurdum."* Let us assume that the people instead of buying the electrical house, bought all of the industrial houses upon which we pay a yearly rental of—say 7½ per cent *ad valorem*. After all, why pick on the electrical house anyway? In Father Marx's home there are many mansions. If the people can "save" twenty-five billion in thirty years on a power investment that will then be worth only twenty billion, they could at the same rate "save," if all business were nationalized and earning an equal return, more money in thirty years than the total national wealth would be worth at the end of that period. Which naturally raises the question, "where did all that money we saved go?"

Of course, the obvious answer to the *absurdum* is that the very money we figured on "saving" is the same money we calculated on being available to buy our government bonds. If all industry were nationalized, of course

there would be no privately earned capital available and we would not be able to sell our bonds at any price. It follows from this also that partial nationalization of industry will *pro tanto* cut down the privately earned capital, and make our bonds correspondingly harder to sell except at a higher rate of interest.

INCIDENTALLY, Mr. Raushenbush has figured in this calculation that our annual rate of rental on the electrical house (which, he estimates, costs us at present $750,000,000) will not be cut down. In this way he figures that we will "save," during the first year, $300,000,000 over and above the payment of $450,000,000 on our government bonds. This would mean that the present level of electrical rates would have to be continued. Surely this assumption, however, is only for purposes of argument. For practical purposes, Mr. Raushenbush assures us that the rates charged by the private industry are too high and that "at the present the public is paying at least $1,000,000 a day more than it needs to pay for light and power." If this be true, the government would owe it to the people to cut the rental by $365,000,000 a year which, deducted from the present return level of $750,000,000, would leave only $385,000,000 profit with which to pay our annual bond interest obligation of $450,000,000. At this rate, the people would be a good deal longer than thirty years paying for their electrical home. The chances are greater that the bondholders would foreclose as certain bondholders are threatening to foreclose on a street railway property in Seattle, which was purchased by that city under plans similar to those outlined by Mr. Raushenbush.

THE principal difficulty with Mr. Raushenbush seems to be that he suffers from all the astigmatisms peculiar to a zealot. The effect of this unbalanced attitude is reflected in the following passage:

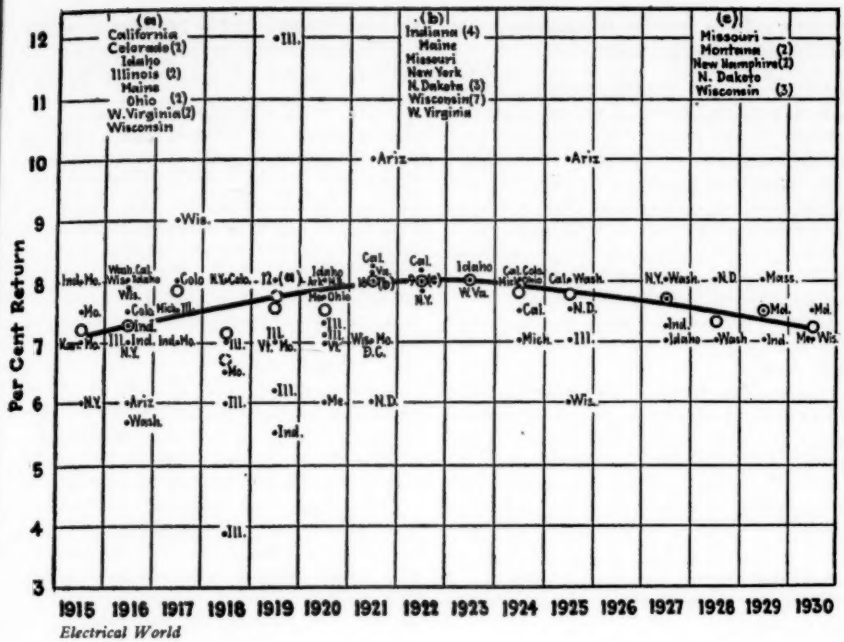
> "A certain amount of decent human sympathy ought to be available for the young men and women who are employed by the utilities and then put into those positions . . . where they are forced to become slick and crafty liars. It is not a very decent life for honorable people and some of them know it. The one man who spat it all out, in confidential letters to a friend, who called his superiors crooks, masquerading patriots, and the like, ended his life not long after his own views became known to the country and to his superiors. It was an impossible situation for him. He had been brought up to expect something better. His trouble was idealism. Not all people are troubled that way. Future generations may have an easier time of it. If the teachers and ministers of the country would only stop giving the young people ideals about life they might get on much more comfortably."

One wonders that Mr. Raushenbush's sense of humor did not cause him to strike out the above paragraph when the first proofs came back from the printer. If one were to take this passage seriously, this reviewer thinks, with all due respect to the author, that it would severely tax the limitation of one's normal common sense.

THE author goes on to tell how the power industry has not only become itself centralized through the process of mergers until it is in the hands of four groups, but has also worked its poisonous way into the balance of our industrial life, until it today dominates the press, the little red schoolhouse, farms, and both political parties. Can it be possible that this single industry, representing an investment of only ten billion in a country whose total national wealth is estimated at four hundred billion, is really running the country, and dictating to the butcher, baker, and candlestick maker?

Are the princes of steel, and the barons of great manufacturing enterprises, taking their orders from the "power trust?" Mr. Raushenbush does not say so. He stops at the brink of his own conclusions. His reasoning leads him up to a point where he almost suggests that the power industry permeates and dominates every type of business in the country.

Something—probably his own com-



This chart shows the rise and fall of return allowances by state commissions in all decisions rendered between 1915 and 1930, inclusive.

mon sense—stops him. But he does not say so—he is satisfied to hint as follows:

> "This account started out to be something more than the story of the power fight. It started out to be the story of the rise in our country of a group which has been outstandingly active in converting those with whom it came into contact into adherents of the new industrial feudalism. That conversion has not been brought about on a particularly high level of religious expression. The converts are largely captives."

MR. Raushenbush seems to be somewhat inconsistent or confused in assessing the blame for the failure of regulation. He says in one place that the commissions have been lax and have let utilities get away with murder. He intimates that many of them are corrupt. Again, he says that the courts are to blame and proceeds to cite decision after decision in which the courts—particularly the Federal courts—have, in these very proceedings *restrained the enforcement of state commission rate orders.* Here is a typical statement condemning the state commissions:

> "At this point the commissions seem to have let down the public through indifference. They have rarely looked at the cost of money in the open market. They accepted the cost of money during the war, which was high, and allowed the utilities to charge the consumers the same high rent in all the years since then, during which the cost of money has been lower. This was neglect of the public interest."

It so happened that during the same week in which Mr. Raushenbush's book was published, the *Electrical World* published a chart showing the rise and fall of return allowances by state commissions in all decisions between 1915 and 1930, inclusive. This chart (reproduced on this page) is not a matter of opinion. It is based on reported de-

cisions. It is an effectual answer to Mr. Raushenbush's accusations.

SUMMING all of the author's arguments up, it would appear that the leaders of the power industry have systematically and deliberately defrauded the American public and plan to continue to do so. If this be true, we have alternative explanations: (1) All business men are devoid of moral sense, or (2) just the electrical business magnates are the industrial crooks.

If the first conclusion is true, then we are, indeed, fallen on evil days, for the corporate immorality of our business leaders would surely be but the outward expression of the innate moral deficiency of the *genus homo*, given only an opportunity to demonstrate itself. It would follow from this that governmental operation would be just as likely, or even more likely, to result in public oppression, for if all men are knaves at heart, how can control by a whole government of such beings reduce dishonesty?

As to the second point, our common sense tells us that there can be no mystic influence of the electrical business which turns an honest man into a villain as soon as he associates himself with it. The electrical business is probably no more honest or dishonest than the oil business or the coal business.

BUT Mr. Raushenbush has the strength of his weakness. In his zeal for preaching the crusade against power, he has searched every nook and cranny for information and evidence. His factual data is widespread and accurate; it is only his interpretations that must be scrutinized. In his criticism of the holding companies, of capitalization of franchises, of intercorporate manipulation of operating expenses, Mr. Raushenbush raises many fair questions which it is the duty of power industry spokesmen either to answer, or plead guilty of and clean house.

The book is well written and has a complete list of references and index. Utility executives would do well to buy and read it. It is the complete indictment against them; it is their enemy at his worst. This reviewer read every word of it and enjoyed it immensely.

—JOHN TRACY FLEMING

THE POWER FIGHT. By Stephen Raushenbush. New York: New Republic, Inc. $1.00. 1932.

7 TO 8 PER CENT A RULING RATE OF RETURN. *Electrical World*. April 2, 1932.

The Swing of the Pendulum Toward and Away from the Centralization of Utility Companies

BEFORE the black autumn of 1929, promoters of public utility holding companies used to make out a strong case for their projects.

Now in the spring of 1932 the situation is changed completely.

Investors in holding company securities have lost fortunes. Does this show that the holding company is the drawback—the greatest structural weakness of the public utility industry today?

That, in brief, was the position taken by Professor James C. Bonbright at the Round Table Conference on Regulation recently held in New York city. Professor Bonbright believes that the downfall of the utility holding company from its former high financial place was caused mainly by three evils; irrational consolidation, overcapitalization, and uncontrolled service charges. He conceded that the holding company has performed a helpful service in consolidating small and far-flung operating units into more economical centralized systems. He added, however:

> "But having done its good work, the holding company has been proceeding for the last decade to undo it with even greater rapidity. For it has carried combination

to a point far beyond that of maximum economy. Normal growth has given way to giantism with the result that a system such as the Electric Bond and Share system or the Insull system must be regarded as an economic disease. Not only is the size of such a system excessive; what is more serious is that it sprawls out on the public utility map of the country without relation to the requirements of physical integration.

"The argument that the tie-up under a great holding company of properties as far apart as those of Maine and California is justified by the theory of diversity of risk is a feeble argument, indeed. One might as well propose to combine the finances and management of the city of New York with the city of Los Angeles on the same theory."

GOING on to the evil of overcapitalization, Professor Bonbright found that the securities of a holding company, formerly regarded more favorably by investors than the securities of its subsidiaries, have since 1929 fallen far below the level of prices fetched by the subsidiary stock. Today the holding company, originally regarded as constituting the great fund-raising device of the operating company, is the "financial weak sister." This situation, according to Professor Bonbright, reflects overcapitalization. Holding companies, free from control, have made the most of their opportunities.

"Fair weather financing," he said, "characterized nearly all holding companies. Now comes foul weather and they are in trouble."

In concluding his analysis of holding company troubles, Professor Bonbright's remarks about the service charge were succinct and severe. He said:

"How any men with a high sense of business honor can support the prevailing system of service contracts, which permits the executives of the parent concern to dictate the prices at which the subsidiaries shall buy services from the holding company, and, therefore, from themselves, is more than I can see. The evil should not be temporized with or merely mitigated. It should be cut out, root and branch. The profit-making service charge must go."

MR. Harper Leech, the last chapter of whose recent book, entitled "The Paradox of Plenty," appears in the current issue of *Review of Reviews*, for example, concedes that our general economic life is due for a program of decentralization. But he goes a step further and states that the decentralizing process of our general industrial life will be in direct proportion to the further centralization of our power production. Viewed in this light, interconnected power systems from Maine to California would not be ludicrous but desirable if and when our technical advances make such coördination economically feasible. Mr. Leech writes:

"This new decentralization is, however, also in part a process of concentration. Production of industrial power is centralized more than before, but this concentration of power generation for the purposes of the utmost and widest availability of power, is a most economical form of concentrated economic activity. As electrical power moves itself from the place of generation, the centralization of its production involves less transport of fuel and materials—less mechanical movement of all sorts—than any other industrial tactic. Because centralized power production now makes possible the application of adequate power at practically any point in the country, other productive processes can be and are being dispersed."

CONCERNING the need for "the new decentralization," Mr. Leech believes that the big city is an "economic absurdity." Its inhabitants pay fortunes in labor, power, and money to keep out of each other's way. It costs as much to move a box of oranges from Jersey City to the Manhattan market as it does to gather, sort, pack, and ship the crop from California to Jersey. Mr. Leech continues:

"Superficially, the greater *per capita* consumption of electricity in cities would indicate higher living standards than in small communities with a lower *per capita* consumption, but much of the urban use of electricity goes merely to level up the city dweller's plane of life to that already enjoyed by the inhabitants of the smaller community without recourse to mechanical power. The economic tides are running so strong against the great city that not even the powerful stimulation it has received from more distributable energy can assure its continued growth, even in suburban form."

Mr. Leech visualizes "a new econom-

ic localism" springing up outside of the great urban belts. The small town will come alive again, literally growing upon the vines of transmission lines rooted in increasingly centralized power production sites. F. X. W.

ADDRESS. By Professor James C. Bonbright before the Round Table Conference on Regulation. New York City. April 8, 1932.

TOWARD A SIMPLER WORLD. By Harper Leech. *Review of Reviews*. April, 1932.

Federal Regulation of Utilities as a Campaign Issue

THE problem of regulating public utility corporations has reached the plane of a major political concern. Not only has effective regulation become an issue in local politics, but it bids fair to become a central issue in the coming presidential election campaign. Today as never before is the general public scrutinizing the results of public utility control. It is, therefore, most appropriate that a scholarly volume on this crucial problem should make its appearance at this time.

Mr. Cassius M. Clay's new book, "Regulation of Public Utilities," deals chiefly with two fundamental aspects of the present-day utility problem. These aspects are: (1) the history and nature of the Supreme Court's views on valuation of public utility properties; and, (2) the mooted question of state *versus* national regulation.

Mr. Clay's views concerning the first problem can be summed up in the following quotations from the work:

> "Under the due process clause of the Fourteenth Amendment, the Supreme Court judicially reviews a wide range of economic and social legislation of the states affecting the rights of persons and property. There is an ever-present danger that this constitutional provision may be used as a vehicle for the freezing into the Constitution of the personal economic and political predilections of individual members who happen to constitute a majority of the court, unless the work of the court is constantly related to the knowledge opened up to the law by workers in the so-called social sciences, such as economics and sociology." (pp. 116, 117).
>
> "The attempt of the majority of the Supreme Court, by the emphasis placed upon reproduction costs, to control commissions' findings of value, represents an excursion by the court into controversial economics. It is further an exercise by the court of economic control under the guise of conceptual legal logic. A recession by the court from the current doctrine of present fair value will leave the duty of fixing rates that are fair from the business standpoint where under a view which has found favor with the court in other days it properly belongs—with the state commissions and other regulatory bodies." (p. 273).

His views on the second point are contained in the following excerpt:

> "At the risk of reiteration, it would seem that hope for improvement lies in the practical laboratories afforded by the forty-eight different states rather than in the rainbow delusion that control of power by a centralized body will usher in a new millennium in so far as rate regulation, or absence of regulation—depending upon the viewpoint—is concerned." (p. 202).

FEW who are familiar with the subject will deny the accuracy of the position taken with reference to the court's valuation doctrine. However, many will probably disagree with the thesis that the Federal government should not engage in effective regulation of public utilities. The position on Federal regulation has been worked out on the basis of the electrical utilities; hence it ignores the pressing problem of interstate transmission of natural gas. Likewise, it ignores the light which experience with the telegraph and telephone industries throws on the problem. What the results of a study based on broader foundations would have been must remain a matter of conjecture. Aside from this point, however, one finds it difficult to follow the theses that Federal regulation could be less effective than present state regulation (p. 198ff), that the regulatory mechanism should be "responsive

to local influences" (p. 190), and that the growth of corporate structures beyond state lines does not call for a higher regulatory authority, more nearly commensurate with the market area of the financial interest, as did the spread of corporate service to several communities call for the transition from local to state regulation. But, on the other hand, one is compelled to grant the force of the contention that:

"Undue centralization results in continual contests for governmental favors between blocks with conflicting selfish interests; the despotism of a dominant section over minority sections; and with the breakdown of party lines and escape from party responsibility." (p. 284).

—KENNETH FIELD,
University of Colorado

REGULATION OF PUBLIC UTILITIES. By Cassius M. Clay. New York: Henry Holt & Company. 309 pages. $3.50. 1932.

Some Unsolved Problems in Consumption Presented by the Age of Electric Power

IN "The Paradox of Plenty" Harper Leech has produced a stimulating study of certain aspects of mass production and the electrical age which ought to be read by politicians and economists as well as by bankers and industrialists.

The professional economist will be forced to reconsider many of the cherished maxims and postulates of the "dismal science" which are clearly demonstrated to be based upon the economics of the pre-steam age and to have little or no reality under present conditions of production and distribution.

The politician, if he has an open mind, will gain a new conception of the futility of legislation which runs counter to the fundamental forces of technological improvement and economic change.

The industrialist, depressed as he may be by present conditions, will be stimulated into renewed optimism by the tremendous opportunities which are being developed through the application of "divisible and distributable electrical energy" to every aspect of modern life and industry.

The banker, if he can withstand the rather caustic criticisms of the banking fraternity which Mr. Leech sets forth in his chapter on "The Pecuniary Priesthood," will be rewarded by a vision of the increasingly important functions which financiers must exercise in an age when credit will necessarily be related ever more closely to energy production rather than to the relatively static gold supply.

THE weakness of "The Paradox of Plenty" lies in its failure to suggest a solution for the paradox which it so vividly presents. This paradox is the situation which Mr. Leech finds in the present business depression where want exists in the midst of plenty and where men and corporations are ruined by the overproduction of valuable things. The remedy is obviously to be found in a change in the distribution of the rewards of industry so that the great masses of the people can purchase in full volume the production of our mines and factories. This has been said in varied phrasing a thousand times by economists, statesmen, and industrial leaders, but neither Mr. Leech nor any one else has told us how we are to attain it in practice. Eighteen months ago it appeared to be accepted as the new American gospel even in the most conservative circles. Today, in the hard realities of the industrial depression and the struggle for self-preservation, the gospel of high wages appears to have little more chance for practical application than the golden rule would have in a bucket shop.

In spite of, or perhaps because of,

this failure to answer the many questions which it raises in its kaleidoscopic picture of the evolution and trend of modern industry, "The Paradox of Plenty" is a challenging and highly stimulating book. The reader may supply his own answers if he chooses but he cannot fail to realize that the problems of the electrical age will be fully as numerous as the opportunities which it creates.

—BASIL MANLY

THE PARADOX OF PLENTY. By Harper Leech. New York: Whittlesey House, McGraw-Hill Book Company, Inc. 204 pages. $2.50. 1932.

The Utterances of Congress About the Utilities

In the Senate

MOTOR CARRIER REGULATION

MR. George (D.) of Georgia obtained leave to have published in the *Record* a comunication which he received from the Georgia Public Service Commission recommending the enactment of legislation empowering the Federal agency to regulate interstate motor carriers. (*April 11, 1932.*)

ECONOMIES AFFECTING RADIO

MR. Dill (D.) of Washington reported back favorably from the Committee on Interstate Commerce a bill (H. R. 7716) with amendments containing two provisions in accordance with the administrative economy program. One is to combine the agencies relating to radio in the Commerce Department and the Radio Commission, and the other is to raise the fees to be paid for the regulation of radio. The revenue expected to accrue would be increased by $670,000 a year. (*April 14, 1932.*)

REGULATION OF POWER

MR. Dill (D.) of Washington obtained leave to have inserted in the *Record* a speech of Governor Franklin D. Roosevelt, of New York, made at St. Paul, Minnesota, April 18th. Governor Roosevelt's speech dealt extensively with power regulation. He commended the efforts of his predecessor, Alfred E. Smith, in frustrating the alienation of the St. Lawrence power rights to private interest. He concluded that utility mergers were too large and that rates for electricity, generally speaking, were too high. (*April 19, 1932.*)

REGULATION OF COAL INDUSTRY

MR. Neely (D.) of West Virginia obtained leave to have inserted in the *Record* various petitions, letters, and telegrams from supporters of the so-called Davis-Kelly coal bill, which would provide for Federal regulation of the bituminous coal industry. (*April 18, 1932.*)

PROPOSED STREET RAILWAY MERGER

MR. Blaine (R.) of Wisconsin obtained leave to have inserted in the appendix of the *Record* a radio address delivered April 18th by Senator Capper (R.) of Kansas, analyzing the proposed street railway merger for the District of Columbia. (*April 18, 1932.*)

HOLDING COMPANY CRITICIZED

MR. Blaine (R.) of Wisconsin obtained leave to have reprinted in the appendix of the *Record* an editorial from the *Capital Times* of Madison, Wisconsin, published April 17th, entitled "The Insull Debacle—Its Significance." The editorial advanced the contention that the Insull smash-up had revealed the inherent weakness of the holding company arrangement, and advocated public ownership as a remedy. (*April 21, 1932.*)

In the House of Representatives

REGULATION OF AIR CARRIERS

MR. Cable (R.) of Ohio spoke in favor of Federal regulation of interstate air carriers. He claimed that unless Congress regulated the commercial air traffic at this time, it would find itself in the same condition in future years as it now finds itself with respect to the absence of motor carrier regulation, which has caused such chaos in the field of land commercial transportation. (*April 9, 1932.*)

INTERSTATE COMMERCE COMMISSION

MR. Crosser (D.) of Ohio spoke in favor of work of the Interstate Commerce Commission, and recommended that its appropriations be sustained. (*April 9, 1932.*)

The March of Events

Round Table Conferees Meet But Fail to Adopt Definite Regulatory Program

THE Round Table Conference on Regulation (announced with names of sponsors in PUBLIC UTILITIES FORTNIGHTLY March 17, 1932, at page 363) met in New York city on April 8th and 9th for a discussion of public utilities and their regulation. Speakers criticized public utility policies and the conferees discussed the problems presented, but they did not reach an agreement on a declaration of policy.

Emphasis was placed upon the subjects of holding companies, Federal and state control, proposed restrictions upon lower Federal courts, valuation, regulatory technique, people's counsels, and accounting.

A report was submitted by the policy committee which analyzed existing regulation and concluded that it fell short of achieving adequately its three major objectives: The protection of consumers, the protection of investors, and the protection of the credit of the utility. Recommendations were made which included the improvement of regulatory technique, the establishment of the prudent investment principle of valuation, revision of present classification of accounts, withdrawal of powers of inferior Federal courts in public utility matters, and a number of other subjects.

The conference voted to receive and not to approve this report on the ground that it had not been submitted sufficiently in advance to the members of the conference to admit of that measure of study and deliberation which an important statement of policy should receive. As there were no members of regulatory commissions on the policy committee, and as some of the regulatory officials present felt that it was not consistent with public duties to subscribe to any statement of policy on matters which might come before them, a caucus was held by such officials and a motion made and carried making the record clear that they had not participated in the preparation or consideration of the report.

Failure to approve the report was taken by the newspapers to indicate a split in the ranks of the conferees. The New York *Times* reported that Professor William Z. Ripley of Harvard University went over to newspaper men and dictated a statement that the report in the form in which it publicly appeared not having been submitted to the conference before issuance, he wished to disclaim any share of responsibility for its form or content. He said that the statement was made without rancor or prejudice but merely in protest against "precipitancy and informality of procedure." Professor Ripley has since stated that press notices gave an unmerited impression of conflict within the group and that while there were differences of opinion as to procedure, there was unanimous agreement on essential underlying issues.

Professor James C. Bonbright of Columbia University led the attack on the holding company organization and development. He conceded that the holding company had performed a service in consolidating the small and competing local utility companies but expressed the opinion that "if unwieldy combination rank first as explaining the change of the holding company from the rôle of public benefactor to that of social evil, overcapitalization and financial mismanagement rank second." Indirectly Professor Bonbright paid a tribute to commission regulation by stating that utility operating companies in a majority of states were subject to financial control by commissions so that their stocks on the whole were not heavily watered, while holding companies, enjoying freedom from control, "have made the most of their opportunity." He also condemned "service charges" made by parent companies for services rendered to their subsidiaries.

Chairman Mayland H. Morse, of the New Hampshire commission, read a paper in which he indicated how the states with appropriate legislation could protect the operating companies against "holding company abuses." Other speakers discussed recent legislation designed to give the state control over holding company regulation.

Commissioner David Lilienthal, of the Wisconsin commission, discussed the improvement of regulatory technique. He referred particularly to (a) necessity for expediting and simplifying regulation, (b) the proper function of the commission, whether judicial or administrative, (c) financing of regulation, (d) judicial review in state and Federal courts, (e) relation between the commission and staff and quality and quantity of the staff, (f) relations between the commission and the public, that is the public relations of the commission.

Expediting of utility rate cases by negotiation in order to avoid delays and uncertainties attendant upon final rate cases, was discussed by Chairman Milo R. Maltbie of the New York commission, and Harold Evans, formerly a member of the Pennsylvania com-

mission, suggested that in view of the fact that the courts, particularly the Federal courts, in confiscation cases require a complete retrial of the facts, it is a waste of time and money for commissions to submit detailed records on value in their own proceedings, and that it might be better to fix rates regardless of value, and then when challenged in judicial proceedings for the first time to put in such detailed and expensive record. Mr. Evans suggested that "we try the experiment of getting away from the idea that our commissions should fix the return to which a utility is entitled as a percentage of a rate base and require them instead to fix rates which will yield a return reasonably sufficient and not more than reasonably sufficient, under proper capitalization, to assure confidence in the financial soundness of the utility and, under efficient and economical management, to maintain its credit and enable it to raise the money necessary for the proper discharge of its public duties." He suggested that book cost be accepted as prima facie evidence of proper capitalization.

It was decided that no formal organization or association would be formed, but that invitations would be extended as occasion warranted for further study.

Alabama

Return of Combined Utilities Is Involved in Rate Case

THE public service commission has taken under advisement the question of a reduction in electric rates of the Birmingham Electric Company. I. F. McDonnell, chief engineer of the commission, recommended approval of a revised schedule which he said would benefit one fourth of the company's 43,000 customers to the extent of $171,000 a year. Representatives of the company vigorously opposed the proposed schedules and a representative of the Alabama Rate Association also assailed the schedule, declaring that it would benefit only large consumers. The association is demanding drastic reductions for all classes.

The question whether the return from the electric and street railway departments should be considered as a whole has been raised. It was testified that the electric department was earning a fair return while the street railway was losing money. J. S. Pevear, president and general manager of the company, insisted that it would be unfair to separate the street car service from other operating units, saying that the city commission, in sanctioning transfer of the franchise of B. R. L. & P. Co. to Birmingham Electric Company in 1924, expressly approved the operation of all the properties and facilities as an integral operating unit. Opponents of the utilities contended that electric consumers should not be required to pay more than a fair price in order to carry the street railway unit.

Commissioner F. P. Morgan inquired whether there was any way for the street car unit, operating alone, to earn a fair return, even on a valuation which permitted a 10-cent fare. Mr. Pevear replied that there was not and Commissioner Morgan then inquired whether the valuation theory did not fall down so far as the street car operation was concerned, to which Mr. Pevear assented.

District of Columbia

Court Is Asked to Standardize Valuation Rules

A NOVEL precedent in standardization of public utility valuation cases will be set by the District Supreme Court, according to the Washington *Post*, if it grants a petition recently filed by the public utilities commission in connection with its present valuation of four local utilities. Granting of the petition would simplify and accelerate the valuation work now under way and all future cases. The *Post* states:

"The petition, covering 310 printed pages, is in reality an amended brief, supplementary to a document filed several months ago. The commission asked for 57 separate instructions and reinforces each request with numerous citations from opinions of the various courts and decisions of the Interstate Commerce Commission."

If the court will set the rules, then the commission will follow them in arriving at the valuations, and the only litigation likely to arise out of future valuation, will be on questions of fact whether the commission did actually follow instructions in a particu-

lar way, says the Washington *Star*, which states that the rulings asked for are to the effect that:

"The present value of the property valued should be considered in determining the compensation to which a utility is entitled; in arriving at a final value, however, the commission is not to be bound by mechanical rules, but must exercise its honest judgment after fair consideration of the several elements of value; consideration must also be given to the original cost of the property, the investment in the property, as well as the reproduction cost of the property.

"The rate base should include only property used and useful, and must exclude abandoned property. Depreciation must be deducted from both original cost and reproduction cost in determining the final value, and the depreciation must be calculated on the 'straight-line' method, by an actual inspection of the units in place and calculation of their probable remaining service lives. Obsolescence should be considered also in determining questions of depreciation.

"A reasonable allowance must be made for working capital. Capitalization is not a proper guide or measure of value nor is capitalization of earnings a proper method of ascertaining value.

"The element of good will shall be left out of the value and so must any 'franchise value,' save money actually spent for acquiring a franchise. There must be some allowance for going-concern value, but none for the cost of developing business.

"No specific allowance must be made for the favorable location of a utility nor for any contracts possessed by the utility nor for the cost of financing."

The commission states that unless it is afforded some clarification of the methods and principles to be applied, it will be obliged to obtain evidence for use under many diverse and conflicting theories of valuation, and that this action would be exceedingly detrimental to the public interest, as it would require an unjustifiable expenditure of public funds, and would greatly prolong the valuation of the properties of the several utilities that have been named as defendants in the proceeding. Such delay would unduly postpone the date of any effective review of rates charged by the utilities and would hamper the commission in the just and reasonable performance of its duties, it is stated.

The companies involved are the Washington Railway & Electric Company, the Capital Traction Company, the Washington Rapid Transit Company, the Washington Gas Light Company, and the Georgetown Gas Light Company.

Cab Driver Not Restricted as to Fare

A TAXI driver may charge any amount he pleases without running afoul of the District law, according to a ruling in traffic court by Judge John P. McMahon, who, according to the Washington *Star*, dismissed a charge against Kenneth Schroyer, a hacker. The *Star* reports:

"B. D. Ladd, 1849 Calvert street, said he entered Schroyer's cab uptown with instructions to be driven to Thirteenth and C streets. There he was informed the charge was 40 cents. Ladd testified Schroyer's cab displayed a 20-cent sign.

"Schroyer maintained he had devised his own system of zones and had run from one zone into another, according to his own way of laying out the city.

"Schroyer was charged with having charged a larger fare than the amount agreed upon. In dismissing the case, the court said the District law does not provide a legal fare."

Florida

Complaint against Telephone Rates Declared to Be Inadequate

A COMPLAINT was recently filed against the rates of the Peninsular Telephone Company in St. Petersburg asserting that rates are unjust and unreasonable and that they are unjustly discriminatory, and in addition, that the telephone company has operated in violation of the law in that it did not publish and file a schedule or tariff showing its charges. The petition seeks a revision of rates.

The company has filed with the state railroad commission a motion for a compulsory amendment to make the charges more specific and to delete one of the charges entirely. It is claimed by the company that the complaint is so framed as to prejudice, embarrass, and delay the fair trial of the action; that one of the paragraphs wholly fails to state any ultimate fact or facts showing or tending to show that any rate or rates of the company are unjust or unreasonable, but merely expresses the assumption, conclusion, and opinion of the petitioners and their counsel. It is further contended that the assertion that the company has violated the law has nothing whatsoever to do, except by implication, with unjust and unreasonable rates. The

company further urges that there are no ultimate facts showing that any rates are unduly preferential, but merely the assumption or opinion of the petitioners and their counsel.

Utilities Tax Law Upheld

CIRCUIT Judge E. C. Love has upheld the validity of the state utilities tax law and dismissed attacks made upon it by seven Florida cities, which operate municipal plants. The law, which was enacted by the 1931 legislature, places a tax of 1½ per cent on gross revenue received by individuals, firms, and corporations, including municipal corporations, for sale or use of electricity and gas for light, heat, power, telegraph, or telephones.

Judge Love ruled that the law imposes an excise tax and not an income tax. The cities had contended that it was an income tax, forbidden by the Florida Constitution. He also held that the tax was not confiscatory. An appeal to the supreme court is expected.

Indiana

Complete Investigation Asked Because of Many Rate Cases

THE Northern Indiana Power Company, which supplies 185 communities and rural areas with electricity, has asked the public service commission to investigate all of its rates and to fix reasonable and nondiscriminatory charges for all of its territory, says the Noblesville *Ledger*, which adds:

"The company in its petition points out that although more than 200 rate reductions have been made in its territory during the last ten years, a number of petitions for further reductions have recently been filed and are now pending before the commission. Interminable delays and expense will be incurred by the public and by the company by a multiplicity of rate cases, the company declares.

"Such delay and expense may be avoided to a large extent, the petition points out, by the commission studying the company's territory as a single operating unit and investigating the whole matter of rates and revenue which the company should receive.

"The company in its petition states that it will, at the proper time, prepare and submit to the commission for its approval schedules of rates which will be just and reasonable and nondiscriminatory.

"The company points out that its rates are now substantially uniform throughout its territory except that communities served are classified into three groups as to the lighting rates, with substantially uniform rates for all of the communities in each group."

The company states that since 1922 the burden of state and local taxes has steadily increased so that persistent and successful efforts toward greater efficiency and economy in the operation of the business, and toward increasing the gross business and thereby reducing the cost per unit to the company and its customers, has been largely nullified by the "unprecedented and grossly unfair and unequitable burden of taxation upon petitioner's property, which burden petitioner and its customers have had to bear." Quoting further from the *Ledger:*

"An analysis of the taxes, excluding Federal taxes, shows that in 1932, the Northern Indiana Power Company will pay taxes amounting to $5.48 per electric customer. This amounts to 45 cents per month in state and local taxes for each customer of the company."

Kansas

Utilities Forego Special Charges

PUBLIC utilities, especially the telephone companies, according to the Topeka *Capital*, have recognized the depression and are reducing some of their service charges, in keeping with a request of the public service commission. The commission several weeks ago sent out a "feeler" to see if the telephone, electric, and gas companies would agree to eliminate, so far as possible, special charges, such as installation and connection tariffs.

The Kansas State Telephone Company has asked and received permission to eliminate its installation and service charges. The Hoyt Telephone Company has received approval of a proposal to discount its bills 50 cents a month on business phones and 25 cents on all others, provided bills are paid

by the 10th of the month. The Kimeo Cooperative Telephone Company dropped its rate of $15 a year to $12. The *Capital* states:

"Several gas companies applied for lower rate schedules for industrial gas. The American Gas Company, Oswego, asked permission to reduce its rate schedule from 65 cents per thousand cubic feet to 50 cents.

"In its application for permission to eliminate its two service charges for old and new business, the Kansas State Telephone Company said: 'This company, like other telephone companies, has suffered considerably from reduced revenue. Believing the time has arrived when it is necessary to take steps to prevent further losses, we contemplate putting into effect a campaign to regain the telephones lost due to economic conditions. We desire to waive the connection charges, from April 1, 1932, to April 1, 1933.'

"The cities affected by the change include Baxter Springs, Galena, Scammon, and Columbus.

"The Ellinwood telephone exchange also received permission to discontinue its installation and connection charges of $1.50 and 50 cents, respectively.

"The Kansas Electric Power Company at Leavenworth asked authority to reduce its minimum charge from 55 cents to 25 cents for large consumers of electricity.

"The Argus Pipe Line and Garden City Gas Company, subsidiaries of the Northern Natural Gas Company, Omaha, asks authority to put into effect a lower industrial rate for large consumers."

Kentucky

Municipal Bureau Makes Recommendations for New Franchise

THE Public Utilities Bureau of Louisville has filed a report containing recommendations for a new franchise in place of the franchise of the Louisville Gas & Electric Company which expires in March, 1933. The return would be 8.20 per cent on the bureau's estimate of the company's valuation.

The report recommends a 20-year franchise, the statutory life of franchises in Kentucky, but from three to five years for the life of the rate schedules.

Under the bureau's proposal electricity would be sold at an average of 5 cents a kilowatt hour and gas at 55 cents a thousand cubic feet. Minimum monthly charges are provided for both gas and electric service, and there are reduced rates per unit for commercial and industrial users, but the minimum bill is larger for these classes.

It is estimated that the new rates would amount to an increase of $313,132 in gas revenues and a decrease of $677,171 in electric revenues. The bureau recommends that gas be supplied at not less than 900 B. T. U. per cubic foot, which, it is said, would mean a constant mixture of artificial and natural gas. The company would be required, without expense to the consumer, to make necessary adjustment of burners and other gas appliances to give the most efficient and satisfactory burning of gas in case of variation of the heating value or pressure at the point of consumption.

There is a proposal that the company should furnish electric service to city institutions on the basis of the commercial rates for lighting and incidental small power, and on the basis of industrial schedule rates for large power service and incidental lighting. The company would be required to bill the combined services of all city institutions as a group for light and power services and not as independent service for each institution.

Some criticism developed after the report was made public. J. L. Stark, secretary-treasurer of the Taxpayers' League, according to the Louisville *Herald-Post*, raised the following points:

"1. Failure to recommend an upset price for the franchise. The present franchise was sold for $25,000 and one promising earnings of upward of six million dollars annually should bring a substantially higher price, he pointed out.

"2. Failure of the report specifically to recommend use of natural gas the year around.

"3. Introduction of minimum monthly bills for both gas and electricity which might, in effect, double present minimum bills to the householder.

"4. Failure to specify graduated rates for both gas and electricity. The report as it stands fixes only 'maximum' rates for both, with no sliding scale.

"5. Fixing the content of gas to be furnished at 900 B. T. U. (British Thermal Units, or the heating capacity of gas) when natural gas now available is capable of producing 1,100 to 1,150 B. T. U."

Massachusetts

Commission Institutes Electric Rate Inquiry

THE state department of public utilities, according to the Worcester *Post,* has started an investigation into the reasonableness and propriety of the rates charged by the Attleboro Steam and Electric Company, the Malden Electric Company, and the Quincy Electric Light and Power Company. This paper adds:

"Several years ago the legislature empowered the department, on its own motion, to inquire into the reasonableness of the rates of any company under its supervision. Until this legislation was enacted into law the department could only inquire into a company's rate structure on application of the mayor of a city, the board of selectmen of a town, or twenty customers.

"Although the department's announcement does not disclose the reason for the investigations, perusal of the companies' annual returns, on file with the department, show that the Attleboro Company paid a dividend last year of 40 per cent, while the Malden Company's dividend rate for 1931 was 27 per cent, and that of the Quincy Company 48 per cent."

Missouri

Therm Basis Used by City Investigators to Compare Gas Rates

A REPORT has been made for the natural gas committee of the St. Louis Board of Aldermen which declares that gas rates in St. Louis are much higher than in cities using natural or mixed gas, which, it is said, results in much less use of gas on the basis of the number of consumers. The report presents comparisons of the cost of gas on the thermal basis. Quoting from the St. Louis *Post-Dispatch:*

"The average cost of gas in St. Louis is given as 17.73 cents a therm (100,000 B. T. U.), compared with 6.25 cents in Cleveland, 5 cents in Columbus, 7.71 cents in Cincinnati, 4.47 cents in Kansas City, and 16.44 cents in St. Louis county. Cleveland, Columbus, and Kansas City have straight natural gas and Cincinnati has mixed gas.

"Not much reduction in cost for general domestic use is to be expected from the rates proposed by the Laclede Gas Light Company for mixed natural and manufactured gas, the report states."

The report states that the rates proposed by the Laclede Gas Company for mixed gas of 800 B. T. U. per cubic foot will not bring the St. Louis cost to anywhere near the cost in the other cities, since in the words of the investigators, "the average reduction of 8.3 per cent will only reduce the average cost to the consumer to 16.26 cents per therm compared to costs ranging from 4.47 cents to 7.71 cents in the other cities, and 16.44 cents under the present and 12.91 cents under the proposed St. Louis county schedules. The composite St. Louis reduction will be greater than above stated if the proportion of house heating and industrial sales is increased.

"Even with the new house-heating rates the cost for gas for that purpose will still be far above the cost of coal and hence the potential field for development will be limited. In Kansas City the revenue from house-heating sales is 10 times the amount in St. Louis. The average cost of gas for this purpose is 5.9 cents a therm; the cost at present in St. Louis is 12.7 cents a therm and as proposed will be 8.9 cents; the cost in St. Louis county at present is 12.8 cents and as proposed will be 8.3 cents."

The investigators attempted to show the underdevelopment of gas use in St. Louis by figures for annual consumption of gas in therms per consumer as follows: St. Louis, 222; Cleveland, 940; Columbus, 1090; Cincinnati, 680; Kansas City, 1,764; St. Louis county, 460.

Another comparison is on the basis of the number of therms of gas the consumer obtains for $1. It is said that this ranges from a low of 5.6 therms per dollar in St. Louis and 6.1 therms per dollar in St. Louis county to 12.9 therms in Cincinnati, which is the next lowest city, and up to 22.4 therms in Kansas City.

The aldermanic committee, it is expected, will use these figures in pressing for a reduction in the rate base valuation of the Laclede Company in rehearing before the public service commission which has been ordered by the state supreme court.

New Jersey

Rates for Hand Phone Sets Excessive, It Is Claimed

COMPLAINT has been made to the public utilities commission that the rate for hand sets, or French telephones, of the New Jersey Bell Telephone Company are excessive and yield too high a return. The rate is 25 cents a month. It was testified at a hearing before the commission that in Washington the hand-set rate had been reduced to 25 cents a month until $4.50 had been paid, after which the service was free. As an alternative the subscriber might pay $4 in cash without the monthly charge.

Counsel for the company asked that the complaint be dismissed on the ground that there was no evidence supporting the assumption that lower rates alleged to be charged in Washington were comparable with those in New Jersey. In reply counsel for the complainant suggested that the board invoke its own power to initiate rate proceedings. Then, according to the Newark *News:*

"Frank H. Sommer, counsel for the commission, advised the board that the rate question raised could be determined only in a formal rate proceeding. This, he said, would require the board to establish a fair value of the property of the telephone company and the return yielded by existing rates."

New York

Commission Power to Regulate Street Lighting Rates Challenged

AN interesting development has arisen in proceedings before the public service commission upon the complaint of Mayor Wilson of the village of Lynbrook, Long Island, against the Long Island Lighting Company and the Queens Borough Gas and Electric Company. At a hearing before Hearing Deputy Krulewitch, counsel for the utilities raised the question whether the Public Service Commission Law gives to the commission power and jurisdiction over rates charged to municipalities for utility service for use in the performance of governmental functions such as lighting the streets.

The provisions of the law relating to the filing of rate schedules specifically exempt "state, Federal, and municipal contracts." The village of Lynbrook refused to make a contract with the utilities on the same basis as practically all other Long Island municipalities, and filed a complaint with the commission, which ordered a hearing.

The hearing deputy ruled preliminarily that the commission had jurisdiction, at least where there is no contract in force, but he indicated the commission's willingness to receive and consider briefs on the questions of law as to jurisdiction. The city of New York, not a party to the proceeding, appeared specially upon this question and its counsel filed a brief supporting the position of the utility companies, contending that the commission had no jurisdiction.

The city of New York makes the following points: That the court of appeals has held that the commission can exercise only such powers as have been specially conferred by statute, together with incidental powers which may be requisite effectually to carry out those actually granted; that the commission has never attempted to take jurisdiction of the subject matter, although in one case it appears to have fixed such rates by the consent of both parties; that the commission itself has refused to take jurisdiction of matters not clearly within the intent of the Public Service Commission Law.

The city counsel argues that the matter of Federal, state, or municipal contracts with public service corporations has been specifically eliminated from the powers granted to the commission, and that these contracts have been distinguished by the legislature from the ordinary business of the lighting companies. It is urged that the city of New York has been granted the power to contract for street lighting in one section of the law, and that there is no other section of the Public Service Law which would apply to the subject matter of street lighting.

The Long Island Lighting Company in its brief states that no one could seriously assert, on the one hand, that the commission's jurisdiction is unmistakably and beyond all doubt negatived and excluded by the statute, or, on the other hand, that such jurisdiction has been recognized and upheld in any clear and controlling decision of the courts or even of the commission itself. It is stated that by no means all of the cities, towns, and villages of the state have evinced accord with the contentions of the mayor of the village of Lynbrook; and that this undetermined question of law is of importance to municipal budgets in many communities. The exigencies of the contentions of a particular village or group of villages ought not, it is submitted, to precipitate a ruling which would lose sight of the "fundamentals of the status

of municipalities in this state and also lose sight of the traditional relationship of the state's *quasi* judicial tribunals to other departments of the state government and to the Federal government."

Penalty Charges Probed

THE public service commission has announced a plan for investigation of the practice of utility companies of charging penalties for slow payment of bills and allowing discounts for prompt payment. This has been undertaken, the commission said, as the result of many complaints from consumers. Gas, electric, telephone, steam, and water companies are included in the inquiry. Proposed rules stating the commission's policy, as reported in the *United States Daily*, are as follows:

"1. The imposition of a penalty in cases where bills are not paid before a fixed date will not be allowed.

"2. Each public utility shall decide in the first instance whether it will or will not allow a discount for prompt payment. Where the utility can collect bills with reasonable promptness without providing for a discount, there should be no discount.

"3. If a utility decides to allow a discount, the bills shall be computed at gross rates and the amount of the discount shown thereon as well as the net amount payable. The date when the bill is rendered, and the date when the discount period expires, shall both be shown.

"The service classification must in each case show the gross rates, the method of determining the discount, and the exact discount period. The net rates may also be shown, if desired.

"4. The discount shall not exceed 10 per cent upon the first $10 of bill (except that the discount may be 25 cents per bill for telephone utilities or 15 cents per bill for other utilities); plus 2 per cent upon portion of bill over $10.

"5. No utility adopting the discount method shall so frame its schedule of gross rates and discounts as to increase the amount of the discount applicable to any customer compared with the discount of penalty under the rates now in effect, without special permission from the commission."

Oklahoma

Appraisal by Two States Proposed

THE Oklahoma Corporation Commission, according to the *United States Daily*, was to ask the Texas Railroad Commission to join in a conference in an attempt to obtain a further appraisal of the properties of the Lone Star Gas Company in order to lower gas rates. This statement was on authority of C. C. Childers, member of the Oklahoma commission.

Chairman Paul A. Walker, of the Oklahoma commission, is reported as saying that he agreed to the move, but not to a reopening of the case, for which he had written an order reducing rates to 62 cents per thousand cubic feet, which order had not yet been signed by either of the other two commissioners. Each of the three commissioners approved different rates.

Pennsylvania

Increase in Water Rates Only Psychological

OFFICIALS of the Scranton-Spring Brook Water Service Company have taken exception to reports made by restaurant and lunchroom owners who announced that large increases in their water rates prompted them to retaliate by throwing out their gas ranges and replacing them with old-fashioned coal stoves. They said that savings on their gas bills would more than offset their increased water bills.

The company officials, according to the Scranton *Times*, state that "there seems to be a psychological belief that water bills have gone up, whereas an investigation will prove that the cost of the same quantity of water now is less" than it was formerly. They said that an inspection of their records would prove that the eating-house owners were harboring delusions inasmuch as many of them were actually paying less for water now than they did under the old schedules.

Under the old schedules a flat rate of 30 cents a thousand gallons was named. Under the new tariff, the charge is 30 cents for the first 75,000 gallons and 20 cents per thousand thereafter. It is declared that thousands of consumers who have been careful have actually reduced their bills. This is said to

be especially true in homes where formerly the owners paid a minimum charge of $2.50 per quarter. Now they pay a service charge of $1.25 plus the consumption rate. Examination of one of the bills of a restaurant owner showed that in one quarter he used 129,000 gallons of water which cost him $34.55, while under the old tariff this water would have cost him $38.70. For other quarters similar comparisons were made.

South Carolina

New Regulatory Bill Signed

THE bill providing for regulation of electric utilities by the state railroad commission has been signed by Governor Blackwood. Under the new law the commission will have jurisdiction over the business of municipal utilities outside the corporate limits of the city. The law also provides for indeterminate franchises for electric utilities and gives jurisdiction to the commission over securities and over fees paid to management and holding companies by operating companies.

Washington

Statewide Probe of Telephone Rates Is Announced

THE state department of public works, according to the Tacoma *Ledger,* has announced that it will immediately undertake a statewide informal inquiry into rates of the Pacific Telephone & Telegraph Company. Resolutions requesting the inquiry have been filed with the department by the cities of Seattle, Tacoma, and Spokane.

The inquiry was to be given a preliminary opening at a round table conference between department officers and official representatives of cities named in the resolution, said Frank Purse, supervisor of public utilities. The department's statement concerning the telephone investigation is in part as follows:

"It is a matter of common knowledge and history that formal proceedings in such matters are costly to the complainants, to the governments of the cities and towns involved, to the state, and to the operating companies. It has been estimated that the last statewide telephone investigation, commenced in 1922 and concluded in 1925 in the Federal court, cost at least $425,000. This cost was, in the last analysis, borne by the people of the state either as taxpayers or as ratepayers. The department is no more desirous of forcing another such charge upon the general public than are the city officials of Seattle, Tacoma, Spokane, and such other cities as may join the city of Seattle in its request."

Wisconsin

Commission Will Oppose Subsidiary Aid to Insolvent Parent

OPERATING utilities in Wisconsin which are controlled by the Middle West Utilities Company, for which receivers have been appointed, will not be permitted by the commission to impair their cash resources for depreciation and other reserves by the payment of dividends or the loaning of money to the holding company, according to a statement by David E. Lilienthal, who said:

"This commission, to the full extent of its power will, in my judgment, not permit the receiver of the defunct Middle West Company to drain off assets of subsidiary public utilities operating in this state for the benefit of the insolvent holding company, whether by way of intercompany borrowings, through the declaration of dividends to the receiver, or by the slighting of depreciation reserves. This was the position taken recently in the case of the Wisconsin Hydro-Electric Company, when its holding company became insolvent, and the commission was successful in enforcing this requirement.

"Our duty is to protect Wisconsin consumers and the investors in the securities of these Wisconsin utilities, and we intend to let nothing stand in the way of this objective. In brief, the insolvency of Middle West Utilities should not adversely affect the people of Wisconsin, except, of course, those who purchased Middle West securities. Those securities are not, under the law, subject to this commission's jurisdiction."

The Latest Utility Rulings

Federal Power Commission Will Investigate and Regulate Florida Power Companies

ACTING on its own motion without formal pleading and wholly because of an informal complaint made by a citizen of Florida through his Congressman, the Federal Power Commission has issued an order addressed to its licensees in Florida upon which the commission entered into an inquiry into the service, rates, and charges of these licensees or their customers engaged in public service. The commission formally declared its intention to exercise jurisdiction granted to it by the Federal Water Power Act of 1921 to control the securities hereafter issued by these licensees in Florida.

The state of Florida will probably be made the starting point for the exercise of these regulatory powers because, as pointed out by the commission's order, the state has no commission or other agency with authority to deal with such a situation. Washington observers saw in the commission's action a commencement of a policy similar to that followed by the prohibition enforcement unit of the Department of Justice, whereby Federal regulation will be brought to bear most actively in those states where there is no local regulation or very little regulation. *Re Ocklawaha Reclamation Farms et al.*

The Equity of a Special Charge to Rural and Suburban Consumers

A PUBLIC utility is not obliged to build an extension, regardless of length, and furnish service to a new customer without expense to him or any additional charge beyond its regular rates, even though it might be able to do so without materially affecting its financial or rate structure. Such was the decision of the Connecticut Supreme Court of Errors in dismissing an appeal by Albert Levitt from a decision of the commission of that state, which in turn dismissed an application of Mr. Levitt to require an electrical utility to extend service about 3,000 feet without extra cost to the applicant above the company's regular rates for service.

Chief Justice Maltbie's opinion pointed out that the utility involved had established a rule to extend service to customers requiring extension lines more than 600 feet in length only under certain conditions, which involved either a guarantee of a certain amount of consumption, or the payment of an extra charge, or the absolute payment for the construction of the extension in excess of 600 feet. Mr. Levitt had contended that the utility was under duty to build such an extension, and to furnish service without any expense to him or additional charge beyond regular rates; or, in other words, that a public utility company was obliged to serve all within the territory in which it is chartered to serve without discrimination in rates, provided it can do so without materially affecting its financial or general rate structure. Justice Maltbie's opinion stated:

> "An examination of the numerous authorities cited by him does not substantiate this claim. A moment's consideration shows that the application of such a principle, at least as applied to a company with charter authority to serve a large rural area, would be impracticable.
>
> "If a company were under a duty to build extensions so long as its financial or

general rate structure was not affected, it could very likely for a time build extensions as they were requested. But a situation would inevitably be reached where the construction of further extensions would affect its financial and general rate structure."

The opinion went on to say that when such a situation arose, the company would either have to refuse to furnish further extensions or follow the very principle already followed by the utility in the case at bar. The court also held that the plaintiff had not properly raised the question of the company's general rate structure so as to make it an issue before the commission or the court. *Levitt v. Public Utilities Commission et al.*

Rate Fixing for Stockyards Follows Utility Practice

ONE of the first comprehensive examples of the exercise of regulatory powers given to the Secretary of Agriculture by the Packers and Stockyards Act of 1921 was provided upon a recent judgment of the Federal District Court reversing certain stockyard rate-fixing orders of the Secretary of Agriculture. The Secretary's order was based upon the value of the stockyard's property and purported to yield a fair return. The court found three reversible errors.

The position of the Secretary was sustained as to the rate of return allowed, which was 7½ per cent, although that was held to be the "constitutional minimum." The court also sustained the contention that Congress had by implications given the Secretary of Agriculture power to value stockyards property.

The first reversible error was the failure of the secretary to include certain lands and other facilities purchased as reasonably required for future expansion in the used and useful property of the stockyards company's rate base. Again the Secretary was held to have erred in requiring the stockyards company to distinguish in its rates for yardage between two different classes of customers. The court thought that this was unwarranted interference with the rights of management. Finally, the Secretary was held to have erred in using the operating statistics of the year of 1929 as a basis for his estimation of future revenue and return. The court felt that a greater period than a year should be used as a basis for the calculation of probable earnings, and a 5-year test period was suggested.

There was another interesting suggestion in the court's opinion to the effect that the Secretary had been rather narrow in excluding small donations from the operating expenses. The Secretary's allowance of going value, based as it was upon 10 per cent of the physical value, was held to be proper as to its computation but unsustainable in the instant proceeding because of the fact that the rate base upon which it was predicated could not be sustained. *Denver Union Stock Yards v. United States.*

Act of God No Excuse for Wholesale Power Interruption

THE Arizona commission found in examining the reasonableness of a contract between the Tucson Gas, Electric Light & Power Company, a wholesale generating concern, and another electrical utility operating a distribution system in Nogales, that during the year of 1931 there were ninety-nine power interruptions aggregating 8,017 minutes, of which the Nogales company had no advance information. The Tucson Company stated most of the interruptions were caused by electric storms, and sought refuge in the fact that it

could not be held responsible for the acts of God. The commission stated:

> "The frequency of the interruptions and their duration strongly indicate that this contention is not sound, particularly in view of the fact that in other sections of Arizona where storm conditions are equally severe and where long-distance transmission lines are maintained, there have been few such unhappy conditions."

The commission found the company's rate to be excessive in its demand requirements and as to the basis for computing the rates with respect to the investment involved in transmission facilities. The commission accordingly ordered the contract to be set aside and fixed the wholesale rates for such service at a greatly modified level. The Nogales company, incidentally, had been forced into the hands of a Federal receiver at the time of the commission's inquiry, as well as at the time of the execution of the contract in question. *Re Tucson Gas, Electric Light & Power Co. et al. Docket No. 4752–E–418, Decision No. 6302.*

Competitive Air Carrier Service, Even without Charge, Is Contrary to the Law

THE Arizona commission has denied the application of an air carrier for a certificate of convenience and necessity to carry passengers and property for compensation by airplane between Phoenix, Tucson, and Douglas, because of the fact that an existing airplane carrier is already operating in the field and the applicant could not make a sufficient showing that public convenience and necessity required the additional service. The applicant had been previously warned against unauthorized operation for hire between the points in question. Following this warning, the applicant ceased to make a charge for such transportation, but it announced that it would carry passengers without compensation. Following this announcement, a large number of persons were handled free of charge. The applicant desired to test the potential traffic between the two cities.

In its opinion denying the application, the Arizona commission stated that this was no test whatever of what the volume of traffic might be under the application of reasonable rates, and it was wholly without weight in that respect since it succeeded only in precluding an actual test that might have been enlightening and helpful. The commission also directed the applicant's attention to § 678, Revised Statutes of 1928, prohibiting common carriers from rendering free service. Commissioner Howe dissented on jurisdictional grounds. *Re Century Pacific Lines, Ltd. Docket No. 4767–L–2481, Decision No. 6311.*

Centralizing of Control of Competing Power Utilities Is Denied

REGARDLESS of whether or not the enactment of the Missouri Public Service Commission Law impliedly repeals the application of the antitrust law of that state to public utilities, the Missouri commission has gone on record as being opposed to centralizing of control of two competing utility companies unless it plainly appears that public interest will be benefited by such change. This ruling came as the result of an application by the Union Electric Light & Power Company for authority to purchase 3,330 voting trust certificates of the Laclede Power & Light Company now held by three members of the North American group, one of which—the Securities Investing Trust —is a "Massachusetts Trust" concern. The Laclede Power & Light Company

is a competitor of the Union Electric Light & Power Company in the city of St. Louis, operating chiefly in the downtown district as a distributor of wholesale power.

The present management of the Laclede Company opposed the granting of the application, emphasizing its own desire and intention of competing with the Union Electric Light Company for further business in St. Louis. The city of St. Louis also opposed the granting of the application. A number of objections were raised as to the granting of the application, including an objection based upon alleged violation of the anti-trust law, but the commission in denying the application, preferred to rest its decision on broader grounds of public policies. The commission stated:

> "These questions and others raised in the brief are important and interesting. To our mind, however, the record discloses a situation which transcends anv of the technical questions involved. In our judgment the application, if granted, would work positive and direct detriment to the public interest and for that reason should be refused."

The commission was of the opinion that the public interest would be jeopardized by the fact that an interlocking directorate would probably result from the granting of the application. On this point, it stated:

> "The present application, if granted, will result in the sanction by this commission of a situation in which the Laclede Company's board of directors will be compelled to include some individual whose natural desires and inclinations will be to further the interest of the Laclede Company's rival and to thwart and hamper the successful operation of the Laclede Company itself. Furthermore, the individual so selected may be, and, as this record discloses, probably will be both an executive officer and a member of the board of directors of the Union Company. He will then be placed in the anomalous and, to the law, insufferable position of owing high allegiance and fidelity to each of two hostile interests."

Re Union Electric Light & Power Co. Case No. 7801.

Jurisdiction of the Commission and a Municipality over Crossing Viaducts

LAST September the Missouri Pacific filed application with the Missouri commission for permission to remove a viaduct over its tracks in Independence, Missouri. The city of Independence filed a protest on grounds that the bridge was still very necessary to carry a certain street over the tracks of the railroad company. Both parties proceeded to produce evidence as to the relative convenience and necessity of the continued maintenance of the structure. The Missouri commission, however, in denying the application and in ordering the city to share the expense of reconstructing the viaduct, rested its decision upon other grounds. The opinion stated:

> "The word 'crossing' can be considered in two senses. In one sense it may be deemed to refer to the abstract, intangible legal right of the public to pass over the tracks on a legally established thoroughfare. In that sense the jurisdiction is entirely the city's. 'It may locate and establish streets whenever and wherever it elects.' But to make this legal right effective so that people can actually cross the tracks in safety, the physical structure is necessary. This physical structure may be also termed a 'crossing.' It is this physical structure that, as we conceive it, the legislature was referring to when it used the word 'crossing' in the statute (R. S. 1929 § 5171). That statute gives this commission complete and exclusive jurisdiction over such structures."

The commission concluded from this that as long as the city permitted the crossing to exist it was its own duty to see that it was maintained in a safe condition for public travel. Both parties were ordered to share in the cost of reconstruction. *Missouri Pacific Railroad Co. v. City of Independence. Case No. 7802.*